



MELBOURNE **IT**

Americas EMEA Asia-Pacific



[melbourneit.info](http://melbourneit.info)

# Momentum:

Shaping a new Internet era

2011

< Annual Report >

## OUR SERVICES

### For small & medium businesses

Domain names, web hosting, web design services, email, search engine marketing, online tools for business

[www.melbourneit.com.au](http://www.melbourneit.com.au)

[www.webcentral.com.au](http://www.webcentral.com.au)

[www.domainz.co.nz](http://www.domainz.co.nz)

[www.advantate.com.au](http://www.advantate.com.au)

### For enterprise & government clients

Online brand protection and online brand performance

[www.melbourneitdbs.com](http://www.melbourneitdbs.com)

Agile, Enterprise-grade IT and infrastructure solutions

[www.melbourneitenterprise.com](http://www.melbourneitenterprise.com)

Digital recording, multimedia and content management solutions

[www.fortherecord.com](http://www.fortherecord.com)

### For partners & resellers

Domain names, web hosting, email and online tools for business

[www.melbourneitgps.com](http://www.melbourneitgps.com)

## AGM DETAILS

The Annual General Meeting (AGM) will be held at:  
Level 2, Spring Street Conference Centre, 1 Spring Street, Melbourne, Australia on Tuesday, 22 May 2012 at 11.00 am.

All shareholders are invited to attend the AGM or to complete and return the proxy form that accompanies the Notice of Meeting.



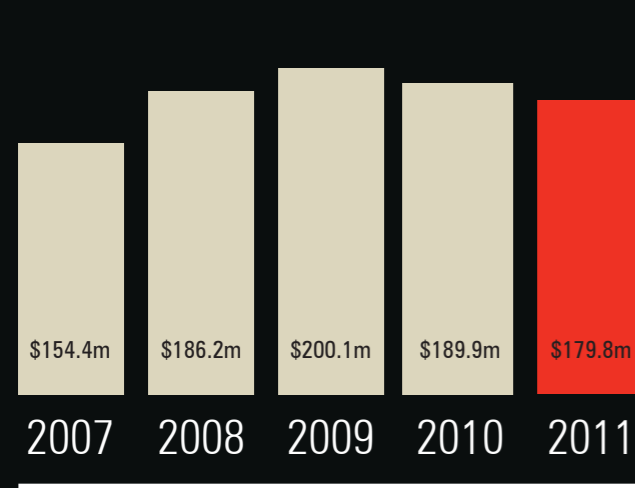
This report has been produced using recycled paper.

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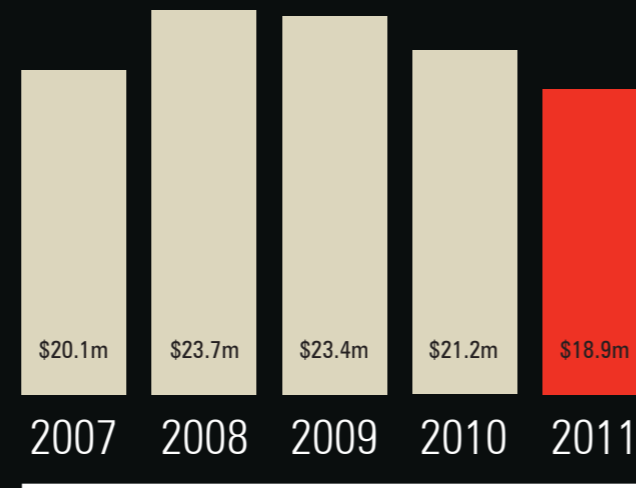
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## Performance over 5 years

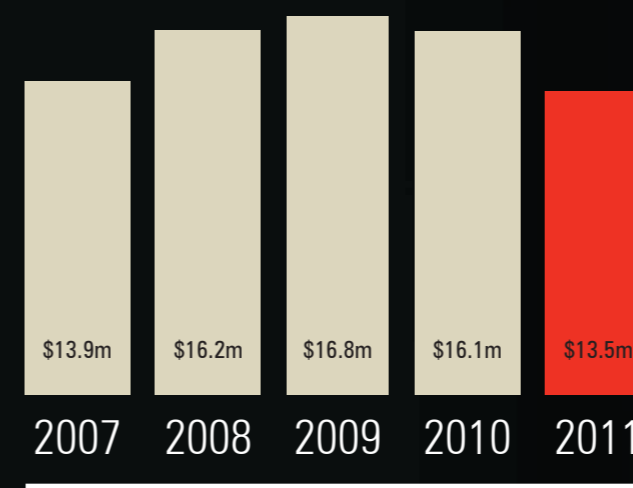
Revenue down  
**5%** to \$179.8m



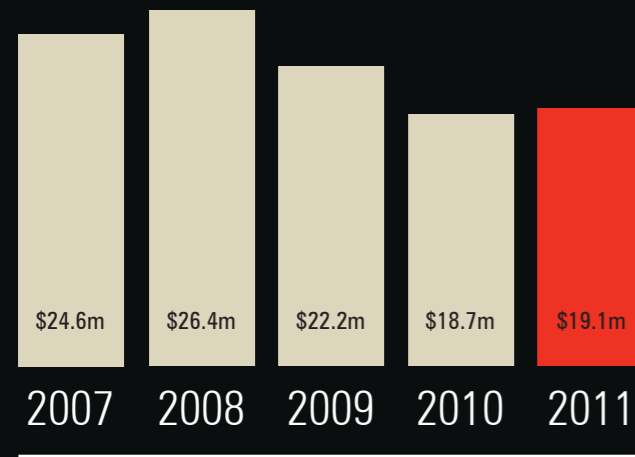
Earnings Before Interest and Tax down  
**11%** to \$18.9m



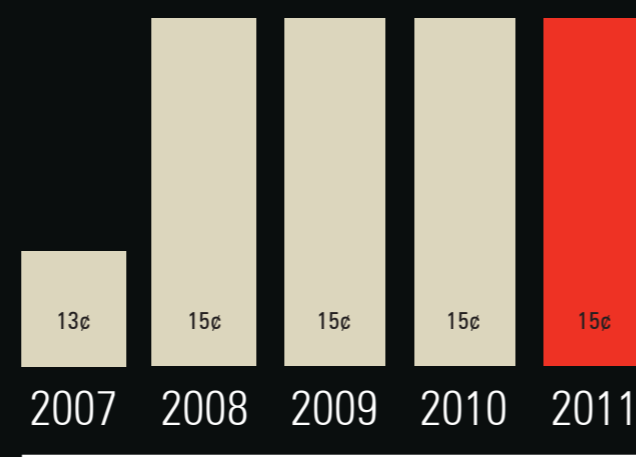
Net Profit after tax down  
**16%** to \$13.5m



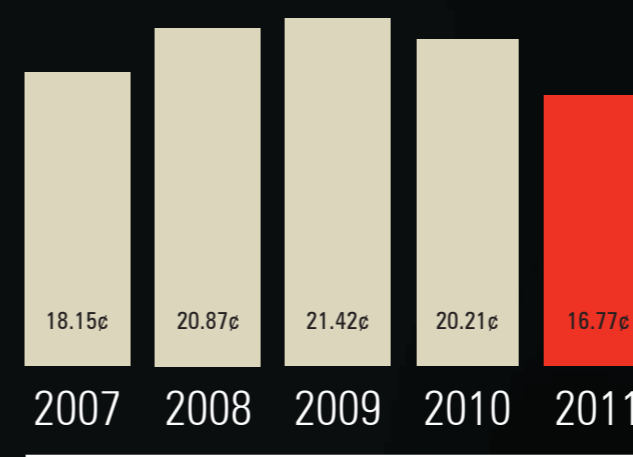
Operating Cash up  
**2%** to \$19.1m



Dividend unchanged  
**15¢**



Earnings Per Share down  
**17%** to 16.77¢



# Chairman's Review Simon Jones



"I believe the much improved second half result provides a true reflection of the earning potential of Melbourne IT and the momentum of this result provides a platform for 2012 success."

On behalf of the Board of Melbourne IT, I am pleased to present the 2011 Annual Report and Annual Review. The Annual Review is a concise version of the past financial year while the complete Annual Report includes all financial details in much more depth. Both are available online at [www.melbourneit.info](http://www.melbourneit.info).

## Our most challenging year

2011 was a year of investment for Melbourne IT – not just in our systems transformation project, but in new products and capabilities to take advantage of the emerging market opportunities for this business. With

the benefits of those investments beginning to flow, and a strong second half of 2011 demonstrating real business momentum, I believe Melbourne IT is set to begin delivering meaningful earnings growth in 2012.

However, 2011 was also possibly the most challenging year in Melbourne IT's 15-year history. The outlay associated with the business investments, a continued foreign exchange headwind provided by a strong Australian Dollar, and a disappointing first half performance contributed to a lower full year result than we had initially expected.

Full year revenue in 2011 was down 5% year-on-year to \$179.8 million, from \$189.9 million in 2010. EBIT declined 11% year-on-year to \$18.9 million, with EBIT being primarily weighed down by the company's increased investment in the Transformation program and an estimated negative foreign exchange EBIT impact of \$2.5 million (based on 2010 rates).

These challenges contributed to a 16% fall in net profit after tax (NPAT) to \$13.5 million in 2011.

However, on an underlying basis Melbourne IT's performance showed bottom line growth. While 2011 revenue was \$187.6 million when restated on a constant currency basis (down 1% year-on-year), underlying EBIT was up 7% to \$24.4 million, taking into account the estimated foreign exchange impact of \$2.5 million and the Transformation operational expenditure (OPEX) investment of \$3 million.

The business continues to generate strong cash flow with a 2% increase in operating cash to \$19.1 million in 2011 from \$18.7 million the year prior. Net debt remains low at \$21.2 million and the company retired \$5.9 million of debt in 2011.

The Board remains confident in the future performance of the business and declared a final dividend of 8c, fully-franked, bringing the full year dividend to 15c. A primary reason for this is the strong second half performance which, we believe, is a sound indicator for the company's prospects in 2012.

## Second half turnaround

After a poor start to 2011, Melbourne IT delivered second half revenue of \$92.2 million, up 5% on the first half revenue of \$87.6 million, and a 70% uplift in EBIT to \$11.9 million compared to \$7 million in EBIT in the first half of 2011.

The second half contribution to NPAT was \$8.6 million, up 76% on the first half NPAT figure of \$4.9 million.

The company's Digital Brand Services (DBS), Enterprise Services and ForTheRecord (FTR) divisions all enjoyed stronger second half performances, with DBS in particular buoyed by a second half EBIT contribution of \$6.2 million. This is almost the equivalent of the division's 2010 full year \$6.4 million EBIT result – despite being negatively impacted by a stronger foreign exchange rate.

Looking back on the past two years of the company's performance, the first half of 2011 stands out as a dip across all financial metrics. I believe the much-improved second half result provides a true reflection of the earning potential of Melbourne IT and a platform for 2012 success.

## 2011 Achievements

While 2011 was a challenging year, there were still notable achievements across the business.

The Transformation project continued in 2011, with Melbourne IT's new Oracle financial system rolled out across the entire business, unifying financial reporting across all locations. The pilot deployment of the company's new billing and customer relationship management (CRM) system was also successfully trialled in the New Zealand operation.

Digital Brand Services staked a legitimate claim to global leadership of the new Top Level Domain (TLD) opportunity in 2011. A compelling service offering, backed by one of the strongest TLD consultancy teams in the industry and a PR campaign which generated more than 1,000 pieces of media coverage across 66 countries, helped the DBS sales team sign more than 120 new TLD contracts in 2011. That number rose to 150 as this report went to print ahead of the 12 April 2012 application deadline.

Leadership, sales and operational changes made in Enterprise Services ensured the division's disappointing first half result was not repeated in the second half. The renewed focus on growing annuity revenue while reducing churn to historically low levels delivered an improved second half and bodes well for 2012.

SMB/GPS, while remaining a strong contributor to the company's EBIT, was hindered by a slowdown in domain registrations by some of the company's largest partners. Pleasingly, however, was the ability for the SMB division to maintain Average Revenue Per User (ARPU) by selling more higher-margin services in a market environment of discounting and commoditisation.

The return of FTR to a positive EBIT contribution was a notable achievement in 2011 and a testament to the investments made in the second half of 2010 to revitalise the sales channel and new product development.

Many of these achievements helped continue Melbourne IT's shift away from domain registration revenue, with IT services and consulting revenue representing 63% of total revenue in 2011, compared to 61% in 2010.

## 2012 Outlook

The extensive investments the company has made in its Transformation program and new product development will begin bearing fruit in 2012.

The company's Transformation program will deliver cost efficiencies and begin benefitting the SMB/GPS divisions this year, helping them maintain the current level of revenue and profitability.

Enterprise Services should continue to grow its annuity revenue base and will leverage its extensive Education market experience to win a greater share of project revenue in 2012. FTR is expected to deliver a similar result this year as in 2011.

DBS displayed its growth potential in 2011 and Melbourne IT expects that growth to continue in 2012. The company's global leadership of the new TLD opportunity will continue, while core brand protection and brand optimisation services should deliver strong revenue.

Assuming the Australian Dollar's value remains the same relative to the US Dollar and major European currencies in 2012, Melbourne IT expects 2012 full year EBIT to be up 10 per cent on 2011.

## With thanks

The employees of Melbourne IT pulled together to deliver a strong finish to 2011 and I thank them for their dedication and tenacity.

I'd also like to thank my colleagues on the Board for their input and influence this year in helping guide Melbourne IT through a year of patient investment.

And finally I would like to thank Managing Director & CEO, Theo Hnarakis, and the Melbourne IT Executive Team for their perseverance during a challenging 12 months to steer this company towards a platform for future growth.

With the array of opportunities ahead I believe Melbourne IT has a prosperous future. I expect 2012 to be the year the company begins delivering on that promise.

**Simon Jones**  
Chairman

# Managing Director's Review

## Theo Hnarakis



“Our investments, coupled with the momentum of the second half of 2011, provide the platform for Melbourne IT to successfully grasp the opportunities set before us this year.”

2011 was a year of mixed fortunes for Melbourne IT.

The successes of 2011 were significant. Melbourne IT established itself as the clear global leader in providing services around ICANN's new Top Level Domain (TLD) program. This leadership, combined with strong growth across key online brand protection and optimisation services, propelled Digital Brand Services to its best profit result to date.

ForTheRecord rebounded from a difficult 2010 to once again deliver a positive EBIT contribution, despite public spending restrictions in its core American market. Enterprise Services also rebounded strongly in the second half, contributing to the group's 70% uplift in EBIT to \$11.9 million compared to \$7 million in EBIT in the first half of 2011.

There were also plenty of challenges. The ongoing strength of the Australian Dollar relative to the US Dollar and major European currencies continued to impact our results and mask the underlying performance of

the business. A slowdown in domain registration by some of our larger partners impacted the revenue of our SMB/GPS division significantly, and some execution challenges in Enterprise Services during the first half contributed to a softer year for that division.

However, our significant investments in Transformation, product and service development, and infrastructure improvements in 2011 position Melbourne IT for long term success and will begin bearing fruit in 2012. These investments, coupled with the momentum of the second half of 2011, provide the platform for Melbourne IT to successfully grasp the opportunities set before us this year.

### New TLD Opportunity 2012 & beyond

The single largest opportunity for Melbourne IT in 2012 continues to be the enormous changes coming to the internet's domain name system in 2013. Already, Melbourne IT DBS has signed contracts to help global brands apply for 150 new TLDs. A full suite of risk assessment, contention and objection consulting services will be available in 2012 to help brands deal with the increasing complexity and potential for infringement associated with the expansion of the domain name system.

In addition to these revenue opportunities in 2012, from 2013 onwards we expect to see a significant rise in registration revenue as the new domains begin appearing on the internet, enhancing DBS's annuity revenue stream.

The knock-on effect to DBS's existing digital optimisation and online brand protection services will also be substantial. We are already seeing the shift among large brands from traditional industries to doing more of their business online, and the introduction of new TLDs will only accelerate the need for quality online insights and strategy.

Online threats to brands are already significant. Phishing attacks – email scams which dupe consumers into providing personal details online – rose 37% between 2010 and 2011. Cybersquatting recovery cases rose 2.5% in 2011 to a record 2,764 cases spanning 4,781 domain names which were held by squatters. Online counterfeiting remains a multi-billion dollar problem. The complexity of this online environment will only increase with the potential introduction of up to 1,500 new TLDs and demand for monitoring and enforcement services will escalate.

Brand threats continue to evolve outside of domains, with malicious software now targeting more than just traditional desktop and laptop computers. The explosion in smart mobile device use – from tablet computers to feature-packed smartphones – has seen the emergence of mobile applications (or 'apps') as a new vector for fraud and brand damage.

In February this year, there was a prime example of this when a fake Pokémon app managed to reach number 2 on the Apple App Store and rake in an estimated \$10,000 before it was removed. In 2012 DBS will launch a new mobile application monitoring service to ensure our clients are protected in this emerging space and their brand is secured.

### Beyond Digital Brand Services

Melbourne IT's prospects in 2012 are not limited to the opportunities for DBS, however.

Despite commoditisation and fierce competition, the Australian SMB market for online services continues to provide significant opportunities. A third of Australian SMBs still do not have a website, and for those that do, understanding how to do business online effectively is an acknowledged challenge by 42% of them.

SMBs are looking for easy-to-use products and advice to help them maximise their online presence and grow their business. With Australian online shopping expected to be worth \$21.7 billion by 2015 and the accelerating rollout of the NBN expected to reach 3.5 million premises by 2015, SMBs continue to invest in their web presence to take advantage of this combination of growing online access and spending.

At the same time, this growth in online access is progressing at a much faster rate in emerging economies globally, and the rapid expansion means an estimated 3 billion people will be online by 2015.

Our SMB/GPS division is ideally placed to capture revenue from both domestic and international trends. Our SMB eBusiness Centres are delivering value-added, higher margin services such as website design, email marketing and search engine marketing (SEM) to help Australian and New Zealand SMBs grow their online capabilities, while our GPS team continues to focus on accelerating partnerships in key emerging markets such as India and the Philippines.

With our systems Transformation project entering its final stages, the ability to deliver the full suite of products to all customers, as well as improve the provisioning and billing of products with both SMB customers and partners, is expected to help SMB/GPS benefit from customer demand faster.

Larger organisations are also investing more heavily in their online operations in Australia as the country's shift from 'bricks to clicks' continues. Woolworths recently publicly stated that it aims to generate \$1 billion of online sales within two years and ensure all its retail brands are trading on the web by 2015, with other large brands following suit with investments planned to bring their online platforms to life. Enterprise Services is set to benefit from this increased investment trend among large corporates by delivering agile platforms which can handle volatile web traffic movements and rapid online marketing campaign deployments.

### An exciting year ahead

2012 promises to be an exciting year for Melbourne IT. While the challenge we face from an adverse foreign exchange rate is unlikely to disappear, the momentum in the business coupled with the benefits of our investments means the company is ideally positioned to capitalise on growth opportunities.

I would like to thank the Board for their continued support and confidence in the direction of Melbourne IT, as well as my hard-working colleagues on our Executive Team. Finally, I would like to show my appreciation for the efforts of all Melbourne IT employees in 2011.

We have a great team, we have a lot to do, but I am confident we have the talent and determination to achieve our goals in 2012.

Theo Hnarakis  
Managing Director & CEO

# Digital Brand Services

## Overview

Melbourne IT Digital Brand Services (DBS) helps corporations manage, protect and optimise their brands online to maximise the value of their digital assets.

As the online business landscape increases in scope and opportunity, the complexity and risk associated with managing digital brands and transacting on the web is also increasing. Hundreds of companies, including some of the world's most recognisable names, trust Melbourne IT DBS to help them manage their online brands.



EBIT grew 41 per cent to a record \$9 million in 2011.

| DBS               | FY11    | FY10    | CHANGE |
|-------------------|---------|---------|--------|
| Revenue           | \$55.3m | \$51.1m | 8%     |
| EBIT Contribution | \$9.0m  | \$6.4m  | 41%    |

## 2011 Highlights

Digital Brand Services delivered a strong result in 2011 with full year revenue up 8% year-on-year to \$55.3 million and EBIT leaping 41% year-on-year to \$9 million. This is the highest EBIT result the division has recorded in its history, despite facing the headwind of a strong Australian Dollar. On a like-for-like constant currency basis using 2010 rates, full year 2011 revenue would have been up 15% to \$58.7 million.

Growth in the second half was robust. Revenue in H2 2011 was \$30.5 million, up 23% on H1 2011 revenue of \$24.8 million. H2 EBIT surged 121% to \$6.2 million from \$2.8 million in H1 2011.

ICANN's new Top Level Domain (TLD) program was approved in June 2011 and DBS quickly built a market leadership position around new TLDs which helped drive the strong second half result as companies sought DBS assistance to develop ".brand" applications.

Core DBS services also grew significantly throughout the year, with Digital Optimisation Services (formally Web Traffic Services) revenue up 74% year-on-year to \$1.6 million, and Brand and Reputation Protection Services revenue increasing 16% year-on-year to \$9.5 million. The number of digital brands under management rose 6% in 2011 to 620,000.

In 2011 DBS's customer base expanded to more than 3,800, with new customers including Dow Corning, Virgin Enterprises Limited and George Weston Foods.

## Outlook

Digital Brand Services entered 2012 with significant momentum as the new TLD opportunity continues to drive revenue in 2012 and beyond. As of April 2012, Melbourne IT DBS has been engaged by leading global brands to manage more than 150 new TLD applications.

As the program moves from the application phase to the evaluation phase in May 2012, DBS will provide new services around managing application risk and contention / objection management to assist brands through the process.

Revenue from the new TLD opportunity will continue in 2013 and beyond, as the increasingly complex domain environment creates greater demand for both brand protection and brand optimisation services, in addition to significant growth in annuity revenues via increased domain registrations.

Threats to online brands continue to grow, with phishing attacks rising 37% in 2011 and online counterfeiting remaining a multi-billion dollar problem. Demand for online brand protection is expected to remain high, and investments in product development will further equip DBS to monetise this opportunity. In 2012 DBS will introduce a search channel monitoring product as well as a new mobile application monitoring service to help organisations combat fraud and phishing attacks via smartphone applications.

DBS's Digital Optimisation Services also stand to benefit in 2012 from the increasing number of companies relying on the internet as their primary route to market, with brands requiring more in-depth online consumer insights to drive their online strategy.

# SMB / GPS

## Overview

Melbourne IT's SMB and Partner divisions (SMB/GPS) delivers online business services to more than 400,000 small and medium-sized businesses in Australia and New Zealand and thousands more worldwide via a global network of 6,900 resellers.

Our eBusiness Centres help small businesses establish and build their online presence via a range of services including domain name registration, email and website hosting, online collaboration tools and eCommerce platforms.

Melbourne IT provides its global partner network with access to a management system to allow resellers to provide domains and value-added online business services to small businesses around the world.

## 2011 Highlights

A 13% decline in domain registration revenue and the effects of the strong Australian Dollar combined to lead revenue of Melbourne IT's small business divisions' – SMB eBusiness Solutions and Global Partner Solutions – 9% lower year-on-year to \$89.4 million. Consequently, the consolidated EBIT contribution for SMB/GPS in 2011 fell 13% year-on-year to \$15.4 million.

A slowdown in major partner activity in the USA contributed significantly to the domain registration revenue shortfall, with partner domains under management falling 12% to 3.6 million names from 4.1 million the year prior.

Despite continued discounting of domains and base level hosting, ARPU among the SMB customer base remained steady at \$301 year-on-year as commoditisation was offset by an uptake in higher-margin online marketing services. Search Engine Marketing (SEM) sales increased 9% year-on-year to \$2.1 million and combined SEM, Software-as-a-Service, and premium email sales grew 2% year-on-year to \$7.7 million.

Following a slow first half, hosting revenue rebounded in the second half of 2011 to \$4.7 million, up 7% on H1 2011 hosting revenue of \$4.4 million.

During the second half of 2011, Melbourne IT successfully piloted the outsourcing of 'Level 1' SMB customer support to consultants based in the Philippines. The success of the pilot in helping improve customer service and reducing support overheads means that all Level 1 SMB support will be outsourced by the end of the first half of 2012.

GPS also continued its expansion into emerging markets in 2011, signing new partners in the Philippines and India.



Despite domain registration revenue declining, SMB ARPU remained steady

| CONSOLIDATED      | FY 11   | FY 10   | CHANGE |
|-------------------|---------|---------|--------|
| Revenue           | \$89.4m | \$98.6m | -9%    |
| EBIT Contribution | \$15.4m | \$17.7m | -13%   |

## Outlook

With Melbourne IT's Transformation project in its final year, SMB/GPS is expected to begin accruing benefits as the year progresses. During the course of the year, an increasing number of products will be made available on the new system and by the end of 2012, the complete suite of SMB products should be available across the entire SMB customer base.

Transformation provides the platform for SMB to deliver a strengthened product portfolio in 2012, including enhanced web design, email marketing and SEM products which target key areas of online investment which SMB customers are demanding. The expansion in delivery of these higher margin services will help further offset the commoditisation pressures facing domains registration and base level hosting revenue.

GPS will continue to expand Melbourne IT's partnerships in emerging markets while accelerating key partnerships which are due to begin delivering services in 2012, including Reckon in Australia.

Melbourne IT is confident that the positive impact of Transformation will help SMB/GPS deliver a 2012 EBIT result in line with 2011, and the division should begin delivering solid growth from 2013 when the full benefits of Transformation will be felt.

# Enterprise Services

## Overview

Melbourne IT Enterprise Services has a strong track record of delivering enterprise-grade Internet services to large organisations.

Hundreds of customers – from blue chip corporations to dynamic media companies and large government departments – rely on our Internet technology platforms and related services to manage customer interactions, manage information, improve productivity and foster innovation.

Our success relies on our deep expertise in the management of hosted and Internet services, our understanding of digital marketing outcomes, our ongoing customer management approach and our ability to define insights and outcomes that create value for our customers.

## 2011 Highlights

It was a disappointing year for Enterprise Services in 2011, with revenue and EBIT both down significantly on the previous year. Revenue decreased 15% to \$26.8 million and EBIT 51% to \$1.7 million, year-on-year. The performance shortfall was primarily due to an absence of large project contracts in 2011, with one off project revenue down 74% year-on-year to \$1.6 million from \$6.2 million in 2010.

However, a strong second half performance – focusing on growing New Monthly Recurring Revenue (NMRR), coupled with a leadership, sales and account management restructure – helped narrow the decline in full year revenue and EBIT. H2 2011 EBIT was \$1.3 million, up 325% on H1 2011 EBIT of \$0.4 million. Cumulative NMRR grew 15% year-on-year to \$507,000 from \$441,000 and customer churn experienced in the first half was reduced 69% in the second half of the year to historically low levels.

Melbourne IT's continued investments in infrastructure and management processes were recognised with ISO9001 Quality Management System Certification in 2011. The infrastructure platform remained very stable, maintaining 99.979% availability for the year.

Enterprise Services signed 182 new contracts in 2011. New customers include Oaks Hotels & Resorts, Cotton On, Credit Union Australia and Colonial First State Global Asset Management.



Enterprise Services is positioned to deliver solid revenue and EBIT growth in 2012.

| ENTERPRISE SERVICES | FY 11   | FY 10   | CHANGE |
|---------------------|---------|---------|--------|
| Revenue             | \$26.8m | \$31.6m | -15%   |
| EBIT Contribution   | \$1.7m  | \$3.5m  | -51%   |

## Outlook

The momentum built in the second half of 2011 provides Enterprise Services with a solid platform for 2012 growth. Growing NMRR remains the focus to ensure the future of Enterprise Services as a long-term, sustainable business is realised.

In addition to growing annuity revenue, Enterprise Services' wealth of expertise servicing the education market ideally positions the division to boost project revenue in this vertical during 2012. Gartner predicts that Australian education technology spend in 2012 will reach \$1.8 billion and will continue to rise at an average rate of 2.7% between 2013-2015. Continued investments in Standards certification will help the business obtain additional government contracts.

Enterprise Services has vast experience in managing agile digital platforms to support customers who need to deal with high online traffic and dynamic customer interactions. The strategic shift towards our new Digital Platform Methodology allows Enterprise Services to create flexible and scalable hosting platforms and associated services to help customers successfully manage online interactions with customers and suppliers.

The accelerating movement by large Australian retailers with traditional 'bricks and mortar' operations towards developing effective eCommerce platforms provides an ideal opportunity for the division to grow its customer base of well-known Australian brands.



# ForTheRecord

## Overview

ForTheRecord (FTR) is a leading global provider of digital recording and content management solutions for courts, law enforcement and government agencies.

FTR provides easy to use, reliable, cost-effective and innovative solutions which enable customers to capture, index, access, review and manage digital audio and video recordings across the organisation, by leveraging a novel and patented annotation linking technology. The technology helps to significantly lower technology infrastructure and transcription costs while improving productivity and efficiency.

FTR has a proven track record of success, providing more than 22,500 digital recording solutions for court rooms, law enforcement and public hearing venues in over 55 countries.

## 2011 Highlights

ForTheRecord saw a return to profitability in 2011 following a challenging 2010. Despite U.S. Public Sector spending remaining constrained, the division reported \$7.8 million in revenue, down 1% year-on-year, and \$1.2 million in EBIT compared to no EBIT contribution in 2010.

On an underlying constant currency basis using 2010 exchange rates, revenue was up 10% to \$8.7 million. A higher proportion of software sales and significant investment in the unit's reseller network helped deliver the improved performance.

Multiple large contracts were won with U.S. government agencies and international customers in 2011, including the roll out of FTR products in 352 court rooms across Slovenia for the Slovenian Ministry of Justice.



An improved 2011 delivered a return to positive EBIT contribution.

| FTR               | FY11   | FY10   | CHANGE |
|-------------------|--------|--------|--------|
| Revenue           | \$7.8m | \$7.9m | -1%    |
| EBIT Contribution | \$1.2m | \$0m   | N/A    |

## Outlook

ForTheRecord expects to maintain revenue and EBIT in 2012 despite the challenging environment for public sector spending in FTR's primary geographic market, the United States.

Supported by the investment in additional product offerings, FTR will continue to push into new international and vertical markets.

The division is also investing in a new consultancy practice to advise courts on best practice for a smooth transition between traditional stenography and the digital capture and management of information. The consultancy arm will be headed by SueLynn Morgan, the former President of the U.S. National Court Reporters Association, who was hired in late 2011.

New product offerings in 2012 are expected to include FTR Notes, the division's first mobile/iPad application and an upgrade to FTR Gold to encompass enterprise capabilities, helping grow new business opportunities.

# Product & Innovation

## Overview

In a world of limitless opportunities, Melbourne IT endeavours to create innovative and dynamic products to help make every online interaction successful. Our investment in product and service development helps our customers deliver a safe and rewarding online experience to their customers.

## 2011 Highlights

Melbourne IT's dedication to innovation and solving customer needs resulted in a number of successful new services launched in 2011.

A complete portfolio of new Top Level Domain (TLD) services was developed in 2011 in response to the approval of the new TLD program by ICANN in June. The initial services launched included TLD Strategy Consulting and Application Management, with Melbourne IT engaged to manage the application for 150 new TLDs at the time of writing. New risk and contention services were also developed for release in 2012 (see Outlook).

The release of the controversial .xxx domain in 2011 was a cause for concern for many of our customers. Melbourne IT became one of a selected number of accredited registrars during the "Sunrise" application period and provided a defensive registration service to our customers to allow them to protect their brand in the new domain space.

As part of our strong relationships with major technology vendors, Melbourne IT was granted exclusive rights in Australia to develop pre-release hosted products for SQL Server 2012, Microsoft's newest version of its popular database product. The SMB eBusiness team created two retail beta products, while Enterprise Services created a dedicated, fully customisable SQL product, which allowed clients to test and verify the utility of SQL Server 2012 on a real world hosted scenario. These offers were released to our global partner network, resulting in the signing up of several beta clients. The official product launch is scheduled for April 2012.

We have continued to build our highly flexible value analytics platform and through work with a large customer, successfully consumed and processed high volumes of data in an extremely short period of time. As a result of these tests, there is potential for the platform to support high demand brand protection applications for DBS. These opportunities will be further explored in 2012.

FTR also saw a strong pipeline of product upgrades and new solutions launch during 2011.

In addition to new product development, investments were made in day-to-day systems. Melbourne IT's quality management systems were recognised with the ISO 9001 accreditation in 2011. Investments in additional operational management systems were made to enhance monitoring of our hosting platform's stability and provide teams with alerts for system changes.

### DIGITAL PLATFORM METHODOLOGY

Enterprise Services' DPM is a structured framework for platforms which experience dynamic online traffic. It ensures companies can successfully manage unpredictable online interactions with customers and suppliers in a safe and reliable environment.

### NEW TLD APPLICATION CONSULTING

The new TLD application consulting service includes complete assembly of required corporate submission information, technical sections of the proposal, and business capability requirements.

### FTR-AS-A-SERVICE PROGRAM

FTR-as-a-Service provides a monthly pay-as-you-go service model for FTR software solutions for law enforcement. The program enables clients to subscribe to services instead of making a large upfront capital investment.

### SOCIAL ACCELERATOR

Social Accelerator assists small businesses to develop a social media presence using Facebook. The pack includes four professionally built and customised commercial Facebook pages; an introduction, coupons, forms and videos, which can then be integrated into the business' website, newsletter emails and business reports.



Melbourne IT has been engaged to complete 150 new TLD applications.

## Outlook

As the convergence and adoption of smart phone and tablet devices continues to rise, the increasing threat of malicious software, malware and other forms of online fraud has also risen. In response, DBS is developing a new Mobile Application Monitoring service to help organisations protect themselves from brand damage via fraudulent mobile applications. This service has been trialled by several large European banks and is set for release in 2012.

New TLD risk management and contention management services are now available to help companies deal with potential infringement and risks associated with the progression of the TLD program to its application evaluation phases. Our application risk review services will help brands identify applications that pose potential risks and provide recommendations, while our contention management services will support brands wishing to file a formal objection against an application during the TLD evaluation process.

Enterprise Services' new Digital Platform Methodology (DPM) provides a robust and flexible framework to Australian enterprises aiming to drive successful online business interactions. DPM will be at the heart of Enterprise Services' agile digital platform offering in 2012 as companies seek to deliver a consistent online end user experience in high volume and unpredictable environments.

With the final stages of the company's new information management systems being implemented during 2012, internal security processes will be further strengthened. Achieving the international standard ISO 27001 as part of this process is one of our goals for 2012, providing a public endorsement of Melbourne IT's industry best practices in maintaining the availability, integrity and confidentiality of data. Enterprise Services' hosting solutions are the target for initial certification.

With more than 700 employees spread across 18 offices in 10 countries, Melbourne IT draws upon a diverse range of skills, abilities and cultural influences to help foster our culture of innovation and success. The human resources (HR) team at Melbourne IT is responsible for providing tools, processes and advice to management across the business to effectively attract, motivate and retain our talented employee base.



## 2011 Highlights

Melbourne IT introduced a number of new work practices, engagement initiatives and career development through training programs in 2011.

Staff in Brisbane, Cape Town and Malmo moved into new, vibrant work environments during the year, with attention paid to creating work spaces that foster collaboration and productivity.

The launch of the internal communication tool, Yammer, across the organisation has also improved interaction between colleagues. The real-time social media application helps staff share knowledge, collateral, news and business opportunities. The introduction of Yammer has been a huge success, with more than 80% of employees signed up and more than 5,400 messages sent to date.

Significant investments have been made to provide training opportunities for staff globally, including extended sales training and the roll out of our highly successful in-house Confident Managers Program to Brisbane and Melbourne offices. More than 3,000 training hours were achieved in 2011.

Continued investments in our people, have enabled us to either promote or move one hundred employees (14 per cent of the workforce) into new roles during the year.

Through further recruitment process improvements, Melbourne IT was able to once again decrease the average days to fill vacancies to a record 33 days. The company also hired a dedicated Internal Communications Manager to assist the company develop and enact a wider employee engagement program.

Melbourne IT is committed to ensuring that its employees and contractors work in an environment that is open, friendly and free of discrimination, harassment and bullying. To ensure employees can work to the best of their ability, Melbourne IT aims to create an environment where employees are treated with dignity, fairness and respect, and where everyone is judged according to merit.

- 65% of employees are male, 35% female. Technical roles, Customer Service and Sales in the IT industry are typically dominated by males. Human Resources, Finance and Legal continue to be dominated by females
- 20% of the executive roles were held by females
- Approximately 29% of managers (with direct reports) were female
- There is a balanced representation of males and females participating in leadership, compliance training and our study assistance program
- In 2011, all employees were required to complete online compliance training courses on Direct and Indirect Discrimination, Melbourne IT Code of Conduct, Harassment and Sexual Harassment
- The company is compliant with equal opportunity legislation administered by the Australian Government's Equal Opportunity for Women in the Workplace Agency (EOWA)

## Outlook

In 2012, Melbourne IT is growing its employee engagement program to further boost productivity and ensure employee understanding of company strategy. Melbourne IT will continue to invest extensively in training.

Investments will be made in improved communication tools, including a revamp of the employee intranet as well as a scheduled program of executive events to increase visibility of senior leaders, while providing more opportunities for staff to provide direct feedback to the executive team.

The company plans to create a new group-wide, peer-nominated awards scheme to further recognise employees for their accomplishments with Melbourne IT. This scheme will supplement existing reward and recognition activities.

A more effective induction process will also be developed to provide staff with a strong understanding of Melbourne IT's objectives, vision and business targets. These improvements aim to improve the on-boarding process for new staff to ensure they become effective contributors in a shorter time.

At Melbourne IT, energy usage is the primary focus for our sustainability efforts as it has a greater environmental impact than other factors for the company due to the nature of our business and our operation of several large data centres.

2011 saw Melbourne IT accelerate its infrastructure life cycle program by upgrading ageing equipment with new, more energy efficient gear.

The hardware refresh, in conjunction with the introduction of automated storage tiering technology, has allowed Melbourne IT to support a larger customer base, thus store more data, while consuming less power.

Efficient systems implemented throughout the year also greatly contributed to Melbourne IT's energy reduction. New backup protection systems assisted with the decrease in tape usage, in turn reducing the amount of electronic waste produced. New operational support systems, which provide a greater level of visibility into our systems, have resulted in more efficient data centre utilisation.

Other efforts have included the installation of new seals on the outer walls of a key Melbourne IT datacentre as well as new air locks on the entrance doors to prevent the loss of cold air.

The company has a policy of selecting more energy efficient equipment when IT hardware is replaced and giving preference to virtualisation wherever possible in order to reduce the amount of hardware in use and subsequently the amount of energy consumed. Melbourne IT is a leader in virtualisation and increased the level of virtualised hardware in 2011 for greater efficiencies.

The impact of these investments in energy efficient data centre technology is magnified when customers choose to outsource their online services with us – instead of using their own (potentially older) equipment they are choosing a more energy efficient solution.

Outside of the data centre, Melbourne IT encourages sustainability efforts in our day-to-day operations.

Employees are encouraged to adopt personal working practices that support energy conservation, such as switching off their PCs and laptops, unused appliances and lights at the end of the day, and printing only what is required. Many processes which were formerly paper-based have now been fully automated.

General recycling facilities for paper and cardboard are provided in all Melbourne IT offices where there are more than ten employees. Where possible, all electronic waste is recycled, re-used or donated to charity to minimise disposable e-waste. Any disposal of electronic waste occurs in accordance with local laws.

Video conferencing technology is also used internally, where practical, to assist in reducing the associated emissions from business travel.

In 2012 we will continue to investigate new initiatives to mitigate the environmental impacts of our operations.

**Simon Jones**  
Chairman



Mr Jones has extensive experience in investment advisory, valuations, mergers and acquisitions, public offerings, audit and venture capital and is a member of the Audit & Risk Management Committee (ARMC) and the Human Resources, Remuneration and Nomination Committee (HRRNC). Mr Jones was appointed Chairman of the Board in November 2009, having served as a Non-Executive Director since 12 March 2003.

**Professor Iain Morrison**  
Non-Executive Director



Professor Morrison is Head of Bond University's School of Information Technology. He was a founding director of Melbourne IT and was appointed to the Board in 1996. He is a member of the Audit & Risk Management Committee (ARMC).

**Theo Hnarakis**  
Managing Director & CEO



Mr Hnarakis was appointed Chief Executive Officer of Melbourne IT in November 2002 and joined the Board on 20 September 2003. Prior to joining Melbourne IT, Mr Hnarakis held senior roles with News Corporation, Boral Group and the PMP Communications Group. He is an IT Fund for Kids Ambassador for the Starlight Children's Foundation.

**Rob Stewart**  
Non-Executive Director



Mr Stewart is a company director and management consultant. Mr Stewart has extensive management and board experience within leading companies across a variety of industries, and was Chairman of Melbourne IT for more than a decade before standing down in October 2009. He is Chairman of the Audit & Risk Management Committee (ARMC).

**Tom Kiing**  
Non-Executive Director



Mr Kiing has extensive experience in mergers and acquisitions, capital markets and corporate finance. He was appointed to the Board on 19 December 2002 and is a member of the Human Resources, Remuneration and Nominations Committee (HRRNC).

**Andrew Walsh**  
Non-Executive Director



Mr Walsh has extensive experience in the global internet industry, primarily in the development of successful online businesses and expanding into new geographies. He was appointed to the Board in June 2008 and is Chairman of the Human Resources, Remuneration and Nomination Committee (HRRNC).

Full details of the Directors' experience, expertise and directorships can be found on the Melbourne IT website at [www.melbourneit.info](http://www.melbourneit.info)

The Melbourne IT Board of Directors recognises the need for the highest standards of corporate behaviour and accountability. The Board is committed to optimising shareholder returns within a framework of ethical business practices.

Melbourne IT corporate governance practices and policies comply with the ASX Corporate Governance Council's revised "Corporate Governance Principles and Recommendations", including the most recent amendments in relation to diversity. This statement reflects a summary of Melbourne IT's corporate governance framework, policies and procedures during the 2011 year.

Further information on the Melbourne IT's corporate governance policies, including Board committee charters, are set out in the Corporate Governance website at <http://www.melbourneit.info/investor-centre/corporate-governance>

### Principle 1 – Lay Solid Foundations for Management and Oversight by Board

Melbourne IT has established functions which are reserved to the Melbourne IT Board and those delegated to senior executives. A statement of those functions is available from the Melbourne IT corporate governance website.

The performance of the Board is regularly evaluated, both formally and informally.

Formal performance reviews are conducted for all staff, including senior executives, on an annual basis. The performance of the senior executives is evaluated on the basis of role descriptions, key performance metrics and 360 degree feedback.

An induction program is conducted for all new Melbourne IT staff, and is accessible for refresher programs for current staff via Melbourne IT's online learning centre.

### Principle 2 – Structure the Board to Add Value

The qualifications of the current Board members are available from the Melbourne corporate governance website.

Four of the five non-executive directors (as at the end of 2011) are considered by the Board to be independent directors (Simon Jones, Iain Morrison, Rob Stewart and Andrew Walsh). Tom Kiing is a substantial shareholder in Melbourne IT, and therefore is not considered by the Board to be an independent director. Theo Hnarakis is the only executive director.

The Chairman, Simon Jones, is an independent non-executive director. The Chairman, and the Managing Director & CEO, are different people.

The Board has an appropriate mix of relevant skills, experience, expertise and diversity, which enables us to discharge its responsibilities and meet its objectives. The Board considers that diversity includes differences that relate to gender, age, ethnicity and cultural background as well as differences in skills, education and functional and industry expertise. A brief biography of each Director is included in the Directors report.

One third of the directors (with the exception of the Managing Director) must retire from office at the time of the Annual General Meeting each year. Directors are eligible for re-election. The directors who retire by rotation are those with the longest period in office since their appointment or last election. The maximum period that a director can be in office before facing re-election is three years. This period will sometimes be shorter due to the requirement that one third must retire each year. At the time when any director is coming up for re-election, the Board considers that question and makes a conscious decision as to whether to recommend that re-election to shareholders.

The Human Resources Remuneration & Nomination Committee (HRRNC) comprises three non-executive directors: Andrew Walsh (Chairperson), Tom Kiing and Simon Jones. Andrew Walsh and Simon Jones are both independent directors. The General Manager, Human Resources and the Managing Director & CEO attend all meetings by invitation. The HRRNC meets at least 3 times a year.

The performance of the Board, its committees and individual directors was informally reviewed during the 2011 financial year. Their performance will next be formally reviewed in the 2012 financial year, with the assistance of an external facilitator.

In certain circumstances a director may consider it necessary to seek independent professional advice in carrying out their duties. Should this arise, the director would discuss the matter first with the Chairman and any advice then considered necessary would be obtained at the company's expense.

### Principle 3 – Promote Ethical and Responsible Decision Making

#### Code of Conduct

The Company has a Code of Conduct to guide the directors, the Managing Director & CEO, the Chief Financial Officer and other key executives as to:

- the practices necessary to maintain confidence in the company's integrity, and
- the responsibility and accountability of individuals for reporting and investigating reports of unethical practices.

Our Code of Conduct is available from Melbourne IT's corporate governance website.

#### Share Trading

The Company also has a Trading Policy concerning trading in company securities by directors, officers and employees involved in material transactions or privy to material information, which complies with the ASX Listing Rules. A copy is available from Melbourne IT's corporate governance website.

#### Diversity

Melbourne IT is committed to ensuring that its employees and contractors work in an environment that is open, friendly and free of discrimination, harassment and bullying. To ensure employees can work to the best of their ability, Melbourne IT aims to create an environment where employees are treated with dignity, fairness and respect, and where everyone is judged according to merit.

- 65% of employees are male, 35% female. Technical roles, Customer Service and Sales in the IT industry are typically dominated by males. Human Resources, Finance and Legal continue to be dominated by females
- 20% of the Executive roles are held by females
- Approximately 29% of Managers (with direct reports) are female
- There is a balanced representation of males and females participating in leadership, compliance training and also our study assistance program

### Principle 4 – Safeguard Integrity in Financial Reporting

The Managing Director & CEO and the Chief Financial Officer have stated in writing to the Board for the 2011 year that the company's financial reports present a true and fair view, in all material respects, of the company's financial condition and operational results and are in accordance with relevant accounting standards.

The Audit and Risk Management Committee (ARMC) comprises four non-executive directors: Rob Stewart (Chairman), Simon Jones and Iain Morrison. The ARMC Chairman is not the Chairman of the Board. The

Chairman of the ARMC is an independent director, as are the majority of other members.

The Managing Director & CEO, Chief Financial Officer and the General Manager, Risk & Audit, attend the meetings by invitation of the ARMC. The relevant partner and staff of Melbourne IT's external auditors also attend by invitation from time to time.

The ARMC meets five times each year and has direct access to Melbourne IT's auditors and senior management. On at least one occasion each year it meets with the auditors without management being present.

The Committee also receives regular reports from both the external and internal auditors concerning any matters which arise in connection with the performance of their role, including adequacy of internal controls. The Committee reports to the Board on its activities after each meeting, and copies of the minutes of the Committee's meetings are provided to all directors.

The ARMC Charter is available from the Melbourne IT corporate governance website.

### Principle 5 – Make timely and balanced disclosure

Melbourne IT is committed to complying with its disclosure obligations. To that end Melbourne IT has developed a written Market Disclosure Policy, which is available from the Corporate Governance section of Melbourne IT's website. The Board has appointed the Company Secretary as "Disclosure Officer", with responsibility for:

- Reviewing compliance with Melbourne IT's continuous disclosure obligations;
- Co-ordination of the timely release of information to the market; and
- Maintaining a record of disclosure information (including any information which was considered but rejected for disclosure and the reasons for non-disclosure).

All market disclosures are reviewed by the directors, together with the Disclosing Officer, to ensure that they are factually correct and complete.

### Principle 6 – Respect the rights of shareholders

Melbourne IT aims to keep its shareholders informed of all important developments concerning the company. Melbourne IT communicates with its shareholders using the following means:

- Notices and explanatory memoranda of annual general meetings;
- The annual report;
- The annual general meeting;
- The Melbourne IT's corporate website located at <http://www.melbourneit.info>
- Periodic analyst briefings, which are released to the ASX; and
- Periodic shareholder announcements, which are also released to the ASX.

Melbourne IT's external auditors attend the Company's Annual General Meeting and are available to answer reasonable questions from shareholders in relation to the conduct of the audit, the independent audit report and the accounting policies adopted by Melbourne IT.

### Principle 7 – Recognise and Manage Risk

The Board has established appropriate policies for the oversight and management of material business risks and a process for management to report as to the effectiveness of the company's management of its material business risks.

Recommendation 7.3 requires the Managing Director & CEO and the Chief Financial Officer to report to the Board that the declaration provided

in accordance with section 295A of the Corporations Act is founded on a sound system of risk management and internal control and that the system is operating effectively in all material respects in relation to financial reporting risks. This recommendation was complied with in 2011 by the Managing Director & CEO and by the Chief Financial Officer.

### Principle 8 – Remunerate Fairly and Responsibly

The Board has established the HRRNC to assist it to address the various issues in this area (see Principle 2 above). The Managing Director & CEO reviews the performance of his direct reports and makes recommendations to the HRRNC for approval in relation to their remuneration and Key Performance Indicators ('KPIs'). The Managing Director & CEO's own performance is reviewed by the Board, facilitated by the HRRNC and the Chairman.

The HRRNC also facilitates an annual review of the Board's performance – both of the Board as a whole and of individual directors.

The HRRNC reports to the Board on its activities after each meeting, and copies of the minutes of the Committee's meetings are provided to all directors.

Melbourne IT's remuneration policy has been set to ensure that the remuneration of directors and all staff properly reflects each person's accountabilities, duties and their level of performance, and to ensure that remuneration is competitive in attracting, motivating and retaining staff of the highest quality. All remuneration packages are reviewed at least annually, taking into account individual and company performance, market movements and expert advice.

Remuneration of non-executive directors in 2011 comprised of a fixed fee only.

Non executive directors are paid fixed fees in accordance with a determination of the Board but within a global limit fixed by the shareholders at a General Meeting. The current global limit of \$1,000,000 was approved by shareholders at the Annual General Meeting in 2008. Approval has not been sought to increase the fees paid to non-executive directors since that date. The Chairpersons of each committee receive an additional amount to reflect (at least to some extent) the additional workload and responsibility required of them to carry out that role.

Directors are not entitled as of right to any retirement or termination benefit (other than statutory superannuation benefits).

The remuneration of the Managing Director & CEO, and executives, comprises the following three elements:

1. Fixed Salary
2. Variable remuneration: short-term incentive
3. Variable remuneration: long-term incentive

The short-term incentive for each executive is an annual cash payment determined by the amount of fixed salary and achievement of individual KPIs. The expected performances of the Managing Director & CEO, staff reporting directly to him (known as 'direct reports') and other senior staff members, are specified each year using Key Performance Indicators (KPIs) in individual role agreements. These KPIs include financial targets for Melbourne IT overall as well as personal objectives and targets, appropriate for each individual's role.

The long-term incentive is membership of the Employee Performance Share Option Plan and/or the Melbourne IT Performance Rights Plan (both of which have been approved by shareholders).

Payment of equity-based executive remuneration is made in accordance with thresholds set in Plans approved by shareholders.

**DIRECTORS' REPORT**

Your directors submit their report for the year ended 31 December 2011.

Directors were in office for the entire period unless otherwise noted.

| Directors           | Managing Director | Company Secretary       |
|---------------------|-------------------|-------------------------|
| Mr. Simon Jones     | Mr. Theo Hnarakis | Ms. Ashe-lee Jegathesan |
| Mr. Tom Kiing       |                   |                         |
| Prof. Iain Morrison |                   |                         |
| Mr. Robert Stewart  |                   |                         |
| Mr. Andrew Walsh    |                   |                         |

**DETAILS OF DIRECTORS' EXPERIENCE, EXPERTISE AND DIRECTORSHIPS**

Full details of the Directors' experience, expertise and directorships can be found on the Melbourne IT website at [www.melbourneit.com.au](http://www.melbourneit.com.au) and the annual report.

**Interests in the shares and options of the company**

As at the date of this report, the interests of the directors in the shares and options of the company and related bodies corporate were:

|                     | Ordinary Shares | Options over Ordinary Shares |
|---------------------|-----------------|------------------------------|
| Mr. Simon Jones     | 125,118         | -                            |
| Mr. Theo Hnarakis   | 688,125         | 773,400                      |
| Mr. Tom Kiing       | 5,721,488       | -                            |
| Prof. Iain Morrison | 53,559          | -                            |
| Mr. Robert Stewart  | 578,744         | -                            |
| Mr. Andrew Walsh    | 48,473          | -                            |

**PRINCIPAL ACTIVITIES**

The principal activities of the Group during the year by operating segment were:

**Digital Brand Services ("DBS")**

- Professional services which enable online brand creation, protection and management, and reputation optimisation across large public and private organisations worldwide.
- Guidance and administration of global domain name portfolios.
- Online brand monitoring, consulting and enforcement.
- Analysis and development of website traffic.

**Enterprise Services ("ES")**

- IT Services, Infrastructure management, hosting and cloud based solutions.
- Data base and application management services.
- Advanced solutions including media content management and distribution, messaging and collaboration services and a unique portfolio of On-Demand Managed Services (ODMS).

**For The Record ("FTR")**

- Develops software and hardware-based digital recording and content management solutions for justice and public safety venues.

**Global Partner Solutions ("GPS")**

Provider of products through the extensive global network of partners which include:

- Registration of generic Top Level Domain (gTLD) names (.com, .net, .org, .biz, .info, .name).
- Registration of .au and .nz domain names through the reseller channel.
- Registration of other country code (ccTLD) domain names (e.g. .us, .co.uk, .fr, .de and .eu).
- Web and application hosting including Software and Services.

**SMB eBusiness Solutions ("SMB")**

- Registration of .au and .nz domain names.
- Registration of other country code (ccTLD) domain names (e.g. .us, .it, .de, .to, .uk and .eu).
- Registration of generic Top Level Domain (gTLD) names (.com, .net, .org, .biz, .info, .name).
- Consultative and fulfilment services for Search Engine Marketing and Web site design and development.
- Website and email application hosting.
- Provision of other Software and Services suited to Small to Medium Business (SMB) and Small Office and Home Office (SOHO).

**DIRECTORS' REPORT (continued)****REVIEW AND RESULTS OF OPERATIONS****EARNINGS PER SHARE**

|                            | 2011        | 2010        |
|----------------------------|-------------|-------------|
| Basic earnings per share   | 16.77 cents | 20.21 cents |
| Diluted earnings per share | 16.60 cents | 20.20 cents |

**RESULTS**

The profit after tax of the Melbourne IT Group for the year ended 31 December 2011 was \$13.524 million (2010: \$16.060 million).

**DIVIDENDS**

|   | Cents | \$'000 |
|---|-------|--------|
| Final Dividend Recommended on ordinary shares | 8.0   | 6,508  |

**DIVIDENDS PAID IN THE YEAR**

|  |     |       |
|--|-----|-------|
| Final Dividend – 2010 on ordinary shares   | 8.0 | 6,404 |
| Interim Dividend – 2011 on ordinary shares | 7.0 | 5,646 |

At the 21 February 2012 Board Meeting, the directors declared a final dividend of 8.0 cents per share, fully franked. The total amount of this final dividend is \$6.508 million. This dividend has not been provided for at 31 December 2011.

**Melbourne IT Ltd - Consolidated Group**

Non-IFRS information included in the summary of results below are unaudited. A table on page 26 shows a reconciliation of the pre- and post-transformation financial results included below to the reported profit after tax, but these performance measures are unaudited except for post-transformation tax expense and profit after tax.

- Total consolidated Revenue for the year ended 31 December 2011 was \$179.778 million (2010: \$189.862 million), a decrease of 5.3%. Revenues for the year ended 31 December 2011 have been significantly impacted by the stronger AUD compared to the same period last year. Revenues for the year ended 31 December 2011 restated using 2010 exchange rates are \$187.643 million (unaudited), equating to a 1.2% decrease on 2010 revenues on a like for like basis.
- Profit after Tax for the year ended 31 December 2011 was \$13.524 million (2010: \$16.060 million), a decrease of 15.8%. Excluding tax effected transformation expense of \$2.098 million (2010: \$1.220 million), adjusted profit after tax was \$15.622 million, a decrease of 9.6%.
- Earnings Before Interest and Tax ("EBIT") for the year ended 31 December 2011 was \$18.911 million (2010: \$21.182 million), a decrease of 10.7%. Excluding transformation expenses of \$2.998 million (2010: \$1.742 million), adjusted EBIT was \$21.909 million (2010: \$22.924 million), a decrease of 4.4%.
- Earnings Before Interest, Tax, Depreciation and Amortisation (EBITDA) for the year ended 31 December 2011 was \$25.036 million (2010: \$28.551 million), a decrease of 12.3%. Excluding transformation expenses of \$2.853 million (total expense less depreciation) (2010: \$1.720 million), adjusted EBITDA was \$27.889 million (2010: \$30.271 million), a decrease of 7.9%.
- Cash and cash equivalents was \$19.047 million at 31 December 2011 (2010: \$23.379 million). At 31 December 2011 total external debt was \$40.291 million (US \$41.0 million) (2010: \$46.246 million (US \$47.0 million)). Net debt is \$21.244 million (2010: \$22.867 million), with the lower external debt offset by lower cash and cash equivalents.
- Positive Operating Cashflow for the year ended 31 December 2011 was \$19.099 million (2010: \$18.729 million), an increase of 2%. Included within the operating cashflow at 31 December 2011 is an interest expense totalling \$1.424 million (2010: \$1.753 million) of which \$1.373 million (2010: \$1.742 million) related to borrowing costs associated with the acquisition of DBMS.
- During the year, Melbourne IT has made quarterly repayments of USD \$1.5m on the USD Overseas Currency loan, a total of USD \$6.0m (AUD \$5.934m).
- Deferred Gross Margin (i.e.: income received in advance net of prepaid costs) was \$29.051 million at 31 December 2011 (unaudited) (December 2010: \$31.599 million) a decrease of 8.1%.
- At the 21 February 2012 Board Meeting, the directors declared an 8.0 cents fully franked final dividend on ordinary shares in respect of the year ended 31 December 2011 (year ended 31 December 2010: 8.0 cents).

**DIRECTORS' REPORT (continued)****REVIEW AND RESULTS OF OPERATIONS (continued)**

- The following table shows a reconciliation of the pre- and post-transformation financial results included on page 25 to the reported profit after tax. The company believes that this non-IFRS information is relevant to the user's understanding of its results, given the significant value of the transformation investment being made.

| Non-IFRS information     | 2011               |                |                     | 2010               |                |                     |
|--------------------------|--------------------|----------------|---------------------|--------------------|----------------|---------------------|
|                          | Pre-transformation | Transformation | Post-transformation | Pre-transformation | Transformation | Post-transformation |
|                          | \$000              | \$000          | \$000               | \$000              | \$000          | \$000               |
| EBITDA*                  | 27,889             | (2,853)        | 25,036              | 30,271             | (1,720)        | 28,551              |
| D & A*                   | 5,980              | 145            | 6,125               | 7,347              | 22             | 7,369               |
| <b>EBIT*</b>             | <b>21,909</b>      | <b>(2,998)</b> | <b>18,911</b>       | <b>22,924</b>      | <b>(1,742)</b> | <b>21,182</b>       |
| Net Interest*            | 1,002              | -              | 1,002               | 1,122              | -              | 1,122               |
| Tax Expense*             | 5,285              | (900)          | 4,385               | 4,522              | (522)          | 4,000               |
| <b>Profit After Tax*</b> | <b>15,622</b>      | <b>(2,098)</b> | <b>13,524</b>       | <b>17,280</b>      | <b>(1,220)</b> | <b>16,060</b>       |

\* An audit opinion has only been provided for post-transformation tax expense and profit after tax.

**Summarised operating results are as follows:**

|  | Note | 2011<br>\$'000 | 2010<br>\$'000 |
|--|------|----------------|----------------|
| <b>Revenue</b>   |      |                |                |
| Registration Revenue   |      | 65,748         | 74,274         |
| Consulting Revenue   |      | 42,414         | 37,620         |
| Hosting & Value-Added Product Sales                          |      | 63,065         | 68,677         |
| For The Record Revenue                                       |      | 7,777          | 7,915          |
| Other Revenue  |      | 342            | 676            |
| Total Revenue excluding Interest Revenue                     |      | 179,346        | 189,162        |
| Interest Revenue   |      | 422            | 631            |
| <b>Total Revenue</b>   |      | <b>179,768</b> | <b>189,793</b> |
| Other Income   |      | 10             | 69             |
| <b>Total consolidated income</b>                             |      | <b>179,778</b> | <b>189,862</b> |
| <b>Earnings Before Net Interest and Tax</b>                  |      |                |                |
| Operating segment results                                    |      | 27,272         | 27,577         |
| Share of loss in Advantate Pty Ltd before income tax expense |      | -              | (20)           |
| Unallocated expenses   |      | (8,361)        | (6,375)        |
| <b>Total Earnings Before Net Interest and Tax</b>            |      | <b>18,911</b>  | <b>21,182</b>  |
| Net Interest   |      | (1,002)        | (1,122)        |
| <b>Net Profit Before Tax</b>                                 |      | <b>17,909</b>  | <b>20,060</b>  |
| Tax Expense  |      | (4,385)        | (4,000)        |
| <b>Net Profit After Tax</b>                                  |      | <b>13,524</b>  | <b>16,060</b>  |
| <b>Cashflow from Operations</b>                              |      | <b>19,099</b>  | <b>18,729</b>  |

**DIRECTORS' REPORT (continued)****RISK MANAGEMENT**

The Group takes a proactive approach to risk management and an active risk management plan is in place. The Group's approach to risk management is to determine the material areas of risk it is exposed to in running the organisation and to put in place plans to manage and/or mitigate those risks.

In addition, risk areas are reviewed by the Group's risk management staff, with consultation of external advisors on specific matters where appropriate, in order to determine the effectiveness of the risk management plan.

Internal audit of key business processes is scheduled across the Group. The entire risk management plan is reviewed at least annually.

**SIGNIFICANT CHANGES IN THE STATE OF AFFAIRS**

During the year, there were no significant changes in the state of affairs.

**SIGNIFICANT EVENTS AFTER THE BALANCE SHEET DATE**

At the 21 February 2012 Board Meeting, the Directors declared a 8.0 cents fully franked final dividend on ordinary shares in respect of the year ended 31 December 2011. The total amount of this final dividend is \$6.508 million, and has not been provided for in the 31 December 2011 financial statements in accordance with the Accounting Standards.

There has not been any other matter or circumstance, other than as referred to in the financial statements or notes thereto, that has arisen since the end of the financial year, that has significantly affected, or may significantly affect, the operation of the consolidated entity, the results of those operations, or the state of affairs of the consolidated entity in future financial years.

**LIKELY DEVELOPMENTS AND EXPECTED RESULTS**

The investments Melbourne IT has made in the transformation project and new services over the past two years, coupled with the compelling DBS opportunity, are expected to deliver strong net growth in 2012. Melbourne IT expects 2012 EBIT to be up approximately 10% on the 2011 result, assuming that the Australian dollar exchange rate remains at current levels. Information on further developments in the Group's operations and expected results of operations have not been included in this report, as the directors believe that this would be likely to result in unreasonable prejudice to the Group.

**INDEMNIFICATION AND INSURANCE OF DIRECTORS AND OFFICERS**

The Company has entered into a Deed of Insurance and Indemnity with each of the non-executive directors and certain officers named earlier in this report and executive directors of controlled entities. Under the Deed, the company has agreed to indemnify these directors against any claim or for any costs which may arise as a result of work performed in their capacity as directors, to the extent permitted by law.

During the financial year, the company paid an insurance premium in respect of a Directors and Officers Liability Policy covering all directors and officers of the company and related bodies corporate. The contract of insurance prohibits disclosure of the nature of the liability and the amount of the premium.

**SHARE OPTIONS****Unissued shares**

As at the date of this report, there were 4,949,104 unissued ordinary shares under options (2010: 5,101,654). Refer to note 33 of the financial statements for further details of the options outstanding.

Option holders do not have any right, by virtue of the option rules, to participate in any share issue of the company or any related body corporate or in the interest issue of any other registered scheme.

**DIRECTORS' REPORT (continued)****SHARE OPTIONS (continued)****Shares issued as a result of the exercise of options**

During the financial year, employees and directors have exercised the option to acquire 92,900 (2010: 174,400) fully paid ordinary shares in Melbourne IT Ltd at a weighted average exercise price of \$1.67 (2010: \$1.21).

In the year ended 31 December 2011 930,000 (2010: 910,000) options were granted over ordinary shares.

The weighted average exercise price per option grant is detailed in the following table:

**Issued Options Outstanding**

| Number of options | Grant date | Vesting date | Expiry Date | Weighted Average Exercise Price |
|-------------------|------------|--------------|-------------|---------------------------------|
| 1,111,000         | 27/04/07   | 27/04/09     | 27/04/12    | 3.42                            |
| 177,066           | 11/09/07   | 11/09/09     | 11/09/12    | 3.60                            |
| 1,433,814         | 18/07/08   | 18/07/10     | 18/07/13    | 3.06                            |
| 142,224           | 19/08/08   | 19/08/10     | 19/08/13    | 3.06                            |
| 405,000           | 24/10/08   | 24/10/10     | 24/10/13    | 2.12                            |
| 180,000 *         | 1/07/10    | 1/07/13      | 1/07/13     | 0.00                            |
| 610,000           | 1/07/10    | 1/07/13      | 1/07/13     | 0.00                            |
| 180,000 *         | 1/07/11    | 1/07/14      | 1/07/14     | 0.00                            |
| 710,000           | 1/07/11    | 1/07/14      | 1/07/14     | 0.00                            |
| <u>4,949,104</u>  |            |              |             |                                 |

\* Represents zero price shares to be settled in cash at time of vesting, offered to international staff.

**DIRECTORS' MEETINGS**

|                             | Directors Meetings |          | Meetings of Committees |    |           |    |
|-----------------------------|--------------------|----------|------------------------|----|-----------|----|
|                             | Eligible           | Attended | ARMC (1)               |    | HRRNC (2) |    |
| No of meetings held in 2011 | 7                  |          | 7                      |    | 3         |    |
| Simon Jones                 | 7                  | 7        | 7                      | 7  | 3         | 3  |
| Theo Hnarakis               | 7                  | 7        | 7*                     | 7* | 3*        | 3* |
| Robert Stewart              | 7                  | 7        | 7                      | 7  |           |    |
| Tom Kiing                   | 7                  | 7        |                        |    | 3         | 3  |
| Iain Morrison               | 7                  | 7        | 7                      | 7  |           |    |
| Andrew Walsh                | 7                  | 7        |                        |    | 3         | 3  |

(1) Audit and Risk Management Committee

(2) Human Resources, Remuneration and Nomination Committee

\* by invitation

The above table shows the numbers of meetings of directors held during 2011. The table also shows the number of meetings attended by each director and the number of meetings each director was eligible to attend.

As at the date of this report, the company had an Audit & Risk Management Committee ("ARMC") and a Human Resource, Remuneration & Nomination Committee ("HRRNC") of the Board of Directors.

The members of the ARMC are Mr R. Stewart (Chairman), Mr S. Jones and Prof. I. Morrison. Mr T. Kiing resigned from the Committee on 1 January 2011.

The members of the HRRNC are Mr A. Walsh (Chairman), Mr S. Jones and Mr. T Kiing (appointed 1 January 2011).

The Managing Director and Chief Executive Officer, Mr Theo Hnarakis attends each ARMC and each HRRNC by invitation.

**ROUNDING**

The amounts contained in this report and in the financial report have been rounded to the nearest \$1,000 (where applicable) under the option available to the company under ASIC Class Order 98/0100. The company is an entity to which the Class Order applies.

**CORPORATE GOVERNANCE**

In recognising the need for the highest standards of corporate behaviour and accountability, the directors of Melbourne IT Ltd support and have adhered to the principles of corporate governance.

The company's corporate governance statement is available on the company's website [www.melbourneit.com.au](http://www.melbourneit.com.au) and is contained in the additional ASX information section of the 2011 annual report.

**DIRECTORS' REPORT (continued)****REMUNERATION REPORT (Audited)**

This Remuneration Report outlines the director and executive remuneration arrangements of the company and the Group in accordance with the requirements of the Corporations Act 2001 and its Regulations. For the purpose of this report Key Management Personnel (KMP) of the Group are defined as those persons having the authority and responsibility for planning, directing and controlling the major activities of the Company and the Group, directly or indirectly.

For the purposes of this report, KMP are the Chief Executive Officer/Managing Director, the Chief Operating Officer, the Chief Financial Officer, the Company Secretary as well as the leaders of Melbourne IT's Global Business Units in Global Partner Solutions ("GPS"), SMB eBusiness Solutions ("SMB") and Digital Brand Services ("DBS"). Directors of the company are also included in the definition of KMP.

**Human Resources, Remuneration and Nomination Committee (HRRNC)**

The HRRNC is responsible for determining and reviewing remuneration arrangements for the directors and executives.

The HRRNC assesses the appropriateness of the nature and amount of remuneration of directors and executives on a periodic basis by reference to relevant employment market conditions and the overall objective of ensuring maximum stakeholder benefit from the retention of a high quality, high performing director and executive team.

**Remuneration philosophy**

The performance of the company depends upon the quality of its directors, executives and staff. To prosper, the company must attract, motivate and retain highly skilled directors, executives and staff.

To this end, the company embodies the following principles in its remuneration framework for executives:

- Provide competitive rewards to attract high calibre executives;
- Link executive rewards to shareholder value;
- Have a significant portion of executive remuneration 'at risk', dependent upon meeting pre-determined performance benchmarks; and
- Establish appropriate, demanding performance hurdles for variable executive remuneration.

The HRRNC of the Board of Directors of the company is responsible for determining and reviewing compensation policy and arrangements for directors, executives and staff.

Further details of remuneration of directors and KMP are also provided in note 32 of the financial statements.

**Remuneration structure**

In accordance with best practice corporate governance, the structure of non-executive director and executive remuneration is separate and distinct.

**Non-executive director remuneration***Objective*

The Board seeks to set aggregate remuneration at a level that provides the company with the ability to attract and retain directors of the highest calibre, while incurring a cost that is acceptable to shareholders.

*Structure*

The Constitution and the ASX Listing Rules specify that the aggregate remuneration of non-executive directors shall be determined from time to time by a general meeting. The last determination was at the Annual General Meeting held on 20 May 2008 when shareholders approved an aggregate remuneration of \$1,000,000 per year.

The amount of aggregate remuneration sought to be approved by shareholders and the manner in which it is apportioned amongst directors is reviewed periodically. The Board considers advice from external consultants, the fees paid to non-executive directors of comparable companies as well as company performance when undertaking the annual review process.



**DIRECTORS' REPORT (continued)****REMUNERATION REPORT (Audited) (continued)****Fixed Remuneration**

Each director receives a fee for being a director of the company. Each director is expected to be a member of at least one committee. An additional fee is paid for chairing a Board committee in recognition of the additional time commitment and responsibility required.

Non-executive directors have long been encouraged by the Board to hold shares in the company (purchased by the directors on market). It is considered good governance for directors to have a stake in a company on whose board they sit. Details of the shareholding as at the date of this report are disclosed on page 2 of the Directors Report.

The remuneration of non-executive directors for the period ended 31 December 2011 is detailed below.

**Structure**

Details of the nature and amount of each element of the emolument of each non executive director of the company for the financial year are as follows:

Emoluments of non-executive directors of Melbourne IT Ltd:

| 2011<br>Directors   | Short Term<br>Salary &<br>fees<br>\$ | Post Employment<br>Super<br>Cont.<br>\$ | Total<br>\$    |
|---------------------|--------------------------------------|---|----------------|
| Mr Simon Jones      | 176,813                              | 15,913                                  | 192,726        |
| Mr Tom Kiing        | 76,875                               | 6,919                                   | 83,794         |
| Prof. Iain Morrison | 76,875                               | 6,919                                   | 83,794         |
| Mr Robert Stewart   | 86,875                               | 7,819                                   | 94,694         |
| Mr Andrew Walsh     | 86,875                               | 7,819                                   | 94,694         |
| <b>Total 2011</b>   | <b>504,313</b>                       | <b>45,389</b>                           | <b>549,702</b> |

| 2010<br>Directors    | Short Term<br>Salary &<br>fees<br>\$ | Post Employment<br>Super<br>Cont.<br>\$ | Total<br>\$    |
|----------------------|--------------------------------------|---|----------------|
| Mr Simon Jones       | 172,500                              | 15,525                                  | 188,025        |
| Mr Tom Kiing         | 75,000                               | 6,750                                   | 81,750         |
| Prof. Iain Morrison  | 75,000                               | 6,750                                   | 81,750         |
| Mr Robert Stewart    | 85,000                               | 7,650                                   | 92,650         |
| Ms Lucy Turnbull (1) | 75,000                               | 6,750                                   | 81,750         |
| Mr Andrew Walsh      | 85,000                               | 7,650                                   | 92,650         |
| <b>Total 2010</b>    | <b>567,500</b>                       | <b>51,075</b>                           | <b>618,575</b> |

(1) Resigned 10 December 2010

**Executive and senior manager remuneration****Objective**

The company aims to reward executives and senior managers with a level and mix of remuneration commensurate with their position and responsibilities within the company so as to:

- Reward them for company, business unit and individual performance against targets set by reference to appropriate benchmarks;
- Align their interests with those of shareholders;
- Link reward with the strategic goals and performance of the company; and
- Ensure total remuneration is competitive by market standards.

**Structure**

To assist in achieving these objectives, the HRRNC links the nature and amount of executive emoluments to the company's financial and operational performance. All executives have the opportunity to qualify for participation in the Executive Incentive Plan which currently provides a cash incentive where specified criteria are met (including criteria relating to cost control, profitability and cash flow).

Remuneration consists of the following key elements:

- Fixed Remuneration
- Variable Remuneration
  - Short term Incentive (STI); and
  - Long term Incentive (LTI)

The proportion of fixed and variable remuneration (potential short term and long term incentives) is established for executives by the HRRNC. The table on page 33 details the fixed and variable components of the key management personnel of the Group and the company.

**DIRECTORS' REPORT (continued)****REMUNERATION REPORT (Audited) (continued)****Executive and senior manager remuneration (continued)****Fixed remuneration****Objective**

Fixed remuneration is reviewed annually by the HRRNC. The process consists of a review of company wide, business unit and individual performance, relevant comparative remuneration in the market and internally, and where appropriate, external advice on policies and practices. As noted above, the HRRNC has access to external advice independent of management.

**Structure**

Executives are given the opportunity to receive their fixed (primary) remuneration in a variety of forms including cash and fringe benefits such as motor vehicles and expense payment plans. It is intended that the manner of payment chosen will be optimal for the recipient without creating undue cost for the Group.

The fixed remuneration component of the key management personnel is detailed on page 33.

**Variable Remuneration – Short Term Incentives (STI)****Objective**

The objective of the STI program is to link the achievement of the Group's operational targets with the remuneration received by the executives charged with meeting those targets. The total potential STI available is set at a level so as to provide sufficient incentive to the executives to achieve the operational targets and such that the cost to the Group is reasonable in the circumstances. During the year ended 31 December 2011, 85% of the 31 December 2010 STI provision was paid.

**Structure**

In order to determine whether an executive will qualify to receive an STI payment, two hurdles need to be met. Firstly, the Earnings Before Interest and Tax ("EBIT") target set by the Company needs to be met. Assuming this occurs, actual STI awards will be made based on the extent to which specific operational targets are met. If the EBIT target is missed, then the payment for the achievement of any operational targets becomes discretionary and will only be paid if the executive has demonstrated excellent performance in meeting those operational targets. The operational targets are set at the beginning of each year and include both financial and non-financial performance metrics, such as contribution to profit, customer service, IT production and development, product and marketing management, finance, legal and human resources management, risk management and leadership/team contribution, including adherence to company values and behaviours.

Both hurdles are assessed on an annual basis, and reviewed by the HRRNC, and are taken into account when determining the amount, if any, of the STI to be paid to each executive. This assessment process usually occurs within three months of the end of our financial reporting.

**Variable Remuneration – Long Term Incentives (LTI)****Objective**

The objective of the LTI plan is to reward executives, senior management and staff in a manner that aligns this element of remuneration with the creation of shareholder wealth.

As such, LTI grants are made to executives, senior management and staff who are able to influence the generation of shareholder wealth and thus have a direct impact on the Group's performance against the relevant long term performance hurdle.

**Structure**

LTI grants to executives are delivered in the form of options to achieve alignment between comparative shareholder return and reward for executives. LTI plans granted, exercised and lapsed during the year ended 31 December 2011 are shown below.

|                                  | Equity Settled | Cash Settled | 2011 Number                              |
|----------------------------------|----------------|--------------|--|
| Number of Options                | 710,000        | 220,000      | Outstanding at the beginning of the year |
| Grant date                       | 1/07/2011      | 1/07/2011    | Granted during the year                  |
| First Vesting date/Exercise date | 1/07/2014      | 1/07/2014    | Exercised during the year                |
| Weighted Average Exercise Price  | -              | -            | Lapsed during the year                   |
| Fair value of Option             | 1.24           | 1.27         | Outstanding at year end                  |

**DIRECTORS' REPORT (continued)****REMUNERATION REPORT (Audited) (continued)****Variable Remuneration – Long Term Incentives (LTI) (continued)****LTI Plans – 21 April 2006 to 30 June 2010**

The exercise condition for Executive LTI Options issued after April 2006 and before 30 June 2010, are based on the increase in basic earnings per share ('EPS') as reported in the annual financial statements against pre-determined performance targets set by the Board.

Executive LTI Options will vest on a sliding scale so that the amount of options vesting to the individual is dependant on the performance level achieved. Performance is measured over the 24 month period immediately following the grant of the Options, with the following sliding scale applying to the exercise of Executive LTI Options:

- If the minimum annual compound EPS growth rate of 7.5% per annum is not achieved, no Executive LTI Options will vest;
- If the annual compound EPS growth rate is equivalent to 7.5% per annum, 50% of the Executive LTI Options will vest;
- If the annual compound EPS growth rate is equivalent to 12.5% per annum, 100% of the Executive LTI Options will vest; and
- For annual compound EPS growth rate between 7.5% and 12.5% the number of Executive LTI Options which will vest increases pro-rata between 50% and 100%.

**LTI Plans – post 1 July 2010**

The exercise condition for Performance Rights/LTI Deferred Cash Bonus Plans (Performance Rights are further described in this report as zero price options and both plans referred to hereafter as "Options") issued on 1 July 2010 and subsequent issues on a yearly basis, are 50% based on the increase in basic earnings per share ('EPS') as reported in the annual financial statements and 50% based on relative total shareholder return ('TSR') as a performance measure against pre-determined performance targets set by the Board. These Options are granted with a zero exercise price.

The Options will vest on a sliding scale so that the amount of options vesting to the individual is dependant on the performance level achieved. Performance is measured over the 36 month period from 1 January of the respective grant year - 31 December of the respective vesting year and settled on an equity basis, except for overseas executives whom on settlement will instead receive a cash bonus. The following sliding scale applies to the exercise of the Options:

**TSR**

- If the TSR is up to the 50.1 percentile of the companies in the Peer Group, then no Options will vest;
- If the TSR is at the 50.1 percentile of the companies in the Peer Group, then 50% of the Options will vest;
- If the TSR is at the 51st percentile of the companies in the Peer Group, then 52% of the Options will vest;
- If the TSR is at the 74th percentile of the companies in the Peer Group, then 98% of the Options will vest; and
- If the TSR is at the 75th percentile of the companies in the Peer Group, then 100% of the Options will vest.

**EPS**

- If the minimum annual compound EPS growth rate of 7.5% per annum is not achieved, no Options will vest;
- If the annual compound EPS growth rate is equivalent to 7.5% per annum, 50% of the Options will vest;
- If the annual compound EPS growth rate is equivalent to 12.5% per annum, 100% of the Options will vest; and
- For annual compound EPS growth rate between 7.5% and 12.5% the number of Options which will vest increases pro-rata between 50% and 100%.

The company proposes to establish a trust to purchase shares on market and hold them until such time as the Options have vested. Holders would have the option, but not the obligation, to continue to hold their shares in the trust after vesting.

**Company performance and link to remuneration***Company performance and link to short and long term incentives*

The financial performance metric on which STI payments are based is the Earnings Before Interest and Tax ("EBIT") result. LTI's vest on the basis of relative TSR and EPS achievements (refer to page 31 for the structure of STI and LTI rewards).

**Hedging of equity awards**

The Company prohibits executives from entering into arrangements to protect the value of unvested LTI awards. The prohibition includes entering into contracts to hedge their exposure to options awarded as part of their remuneration package.

**DIRECTORS' REPORT (continued)****REMUNERATION REPORT (Audited) (continued)****Emoluments of Executives of the Company and the Consolidated Entity**

Details of the nature and amount of each element of the emoluments of the key management personnel of the company for the financial year are as follows:

| 2011<br>Executives     | Short term benefits |                |               | Post<br>Employment | Long term<br>benefits    | Share Based<br>Payments     | Total            | Performance<br>related |
|------------------------|---------------------|----------------|---------------|--------------------|--------------------------|-----------------------------|------------------|------------------------|
|                        | Salary &<br>fees    | STI            | Other (4)     | Super<br>Cont.     | Long<br>service<br>leave | Amortisation<br>Expense (5) |                  |                        |
|                        | \$                  | \$             | \$            | \$                 | \$                       | \$                          | \$               | %                      |
| Mr Theo Hnarakis       | 568,950             | 148,418        | 38,356        | 47,134             | 18,891                   | 121,890                     | 943,639          | 28.65%                 |
| Mr Damian Walsh        | 294,304             | 40,000         | 10,178        | 25,713             | 3,726                    | 51,438                      | 425,359          | 21.50%                 |
| Ms Lori Harmon (1)     | 236,502             | 19,391         | -             | 4,920              | -                        | 29,146                      | 289,959          | 16.74%                 |
| Mr Damon Fieldgate     | 230,106             | 15,000         | 6,703         | 20,700             | 4,895                    | 34,292                      | 311,696          | 15.81%                 |
| Ms Ashe-lee Jegathesan | 223,705             | 35,000         | 8,084         | 20,619             | 2,787                    | 29,492                      | 319,687          | 20.17%                 |
| Mr Kanchan Mhatre (1)  | 246,806             | 38,782         | -             | 7,247              | -                        | 29,146                      | 321,981          | 21.10%                 |
| Ms Carolyn Sutton (2)  | 200,512             | -              | 7,498         | 5,548              | -                        | (12,000)                    | 201,558          | (5.95%)                |
| Mr Peter Findlay (3)   | 63,142              | 18,333         | 2,440         | 5,548              | -                        | -                           | 89,463           | 20.49%                 |
| <b>Total 2011</b>      | <b>2,064,027</b>    | <b>314,924</b> | <b>73,259</b> | <b>137,429</b>     | <b>30,299</b>            | <b>283,404</b>              | <b>2,903,342</b> |                        |

(1) These personnel are paid in USD equivalents

(2) Ms Carolyn Sutton resigned from the executive as Chief Financial Officer on 23 August 2011

(3) Mr Peter Findlay was appointed to the executive as Chief Financial Officer on 17 October 2011

(4) The category of "Other" includes the value of any non-cash business benefits provided

(5) The expense relates to the amortisation of the fair value of options granted prior to the end of the year ended 31 December 2011

| 2010<br>Executives     | Short term benefits |                |               | Post<br>Employment | Long term<br>benefits    | Share Based<br>Payments     | Total            | Performance<br>related |
|------------------------|---------------------|----------------|---------------|--------------------|--------------------------|-----------------------------|------------------|------------------------|
|                        | Salary &<br>fees    | STI            | Other (8)     | Super<br>Cont.     | Long<br>service<br>leave | Amortisation<br>Expense (9) |                  |                        |
|                        | \$                  | \$             | \$            | \$                 | \$                       | \$                          | \$               | %                      |
| Mr Theo Hnarakis       | 508,581             | 108,387        | 43,001        | 45,894             | 23,013                   | 72,068                      | 800,944          | 22.53%                 |
| Mr Damian Walsh        | 276,309             | 30,000         | 9,522         | 24,715             | -                        | 18,000                      | 358,546          | 13.39%                 |
| Ms Lori Harmon (6)     | 258,238             | 65,236         | -             | 5,424              | -                        | 11,542                      | 340,440          | 22.55%                 |
| Mr Damon Fieldgate     | 209,500             | 7,500          | 6,488         | 20,700             | 4,124                    | 15,320                      | 263,632          | 8.66%                  |
| Ms Ashe-lee Jegathesan | 220,436             | 10,500         | 7,476         | 19,719             | 2,974                    | 9,600                       | 270,705          | 7.43%                  |
| Mr Kanchan Mhatre (6)  | 286,187             | -              | -             | 8,182              | -                        | 16,197                      | 310,566          | 5.22%                  |
| Ms Carolyn Sutton (7)  | 261,082             | 30,000         | 9,387         | 22,518             | -                        | 12,000                      | 334,987          | 12.54%                 |
| <b>Total 2010</b>      | <b>2,020,333</b>    | <b>251,623</b> | <b>75,874</b> | <b>147,152</b>     | <b>30,111</b>            | <b>154,727</b>              | <b>2,679,820</b> |                        |

(6) These personnel are paid in USD equivalents

(7) Ms Carolyn Sutton was appointed to the executive as Chief Financial Officer on 1 February 2010

(8) The category of "Other" includes the value of any non-cash business benefits provided

(9) The expense relates to the amortisation of the fair value of options granted prior to the end of the year ended 31 December 2010

**Employment Contracts**

The Managing Director and Chief Executive Officer, Mr Hnarakis, is employed under contract. The current employment contract commenced in November 2002 and continues until such time that employment is terminated.

- Mr Hnarakis was entitled to receive up to a further 65% of this base remuneration based on achieving annual performance criteria set by the Board.
- Mr Hnarakis' remuneration is reviewed annually.
- Mr Hnarakis may resign from his position and thus terminate this contract by giving 6 months notice.
- The company may terminate this employment agreement by providing 12 months written notice or providing payment in lieu of the notice period (based on the fixed component of Mr Hnarakis' remuneration).

All other key management personnel are on standard contracts and are remunerated as stipulated in this report.

**DIRECTORS' REPORT (continued)****REMUNERATION REPORT (Audited) (continued)****Compensation options: Options granted and Options vested during the year****2011**

In the year ended 31 December 2011 460,000 (2010 : 500,000) options were granted to the KMP.

**Options granted / lapsed as remuneration during the year****2011**

|                        | Options<br>Granted | Value of<br>options granted<br>\$ | Value of options<br>exercised<br>\$ | Number of<br>options lapsed<br>/ forfeited | Remuneration<br>consisting of<br>options (1) |
|------------------------|--------------------|-----------------------------------|-------------------------------------|--|--|
| <b>Executives</b>      |                    |                                   |                                     |  |  |
| Mr Theo Hnarakis       | 185,000            | 228,475                           | -                                   | (250,000)                                  | 12.92%                                       |
| Mr Damian Walsh        | 75,000             | 92,625                            | -                                   | -  | 12.09%                                       |
| Ms Lori Harmon         | 50,000             | 63,276                            | -                                   | -  | 10.05%                                       |
| Mr Damon Fieldgate     | 50,000             | 61,750                            | -                                   | -  | 11.00%                                       |
| Ms Ashe-lee Jegathesan | 50,000             | 61,750                            | -                                   | -  | 9.23%  |
| Mr Kanchan Mhatre      | 50,000             | 63,276                            | -                                   | -  | 9.05%  |
| Ms Carolyn Sutton (2)  | -                  | -                                 | -                                   | (50,000)                                   | 0.00%  |
| Mr Peter Findlay (3)   | -                  | -                                 | -                                   | -  | 0.00%  |
|                        | 460,000            | 571,152                           | -                                   | (300,000)                                  |  |

(1) Amortisation expense of employee share options

(2) Resigned 23 August 2011

(3) Appointed 17 October 2011

There were no alterations to the terms and conditions of options granted as remuneration since the grant date.

The maximum grant, which will be payable assuming that all service and performance criteria are met, is equal to the number of options granted multiplied by the fair value at the vesting date. The minimum grant payable assuming that service and performance criteria are not met is zero.

The exercise price of the options granted during the year is zero. These represent rights to acquire shares given certain performance criteria are met.

**Shares issued on exercise of compensation options****2011**

No shares were issued to KMP's on exercise of compensation options for the year ended 31 December 2011.

**Employees**

The consolidated entity employed 716 full time equivalent ("FTE") employees as at 31 December 2011 (2010:715).

**Auditor independence and non audit services**

The Directors have received an independence declaration from the auditor of Melbourne IT Ltd, as shown on page 35.

**Non audit services**

The following non audit services were provided by the Group's auditor, Ernst & Young. The directors are satisfied that the provision of non audit services is compatible with general standards of independence for auditors imposed by the Corporations Act 2001. The nature and scope of each type of non audit service provided means that auditor independence was not compromised.

Ernst & Young received or are due to receive the following amounts for the provision of non audit services:

|  |               |
|--|---------------|
|  | \$            |
| Tax compliance services                      | 73,178        |
| Assurance related and due diligence services | 24,200        |
|  | <u>97,378</u> |

Signed in accordance with a resolution of the directors.



Simon Jones (Chairman)

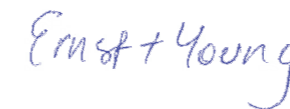
Melbourne, 30 March 2012



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www.ey.com/au

**Auditor's Independence Declaration to the Directors of Melbourne IT Limited**

In relation to our audit of the financial report of Melbourne IT Limited for the financial year ended 31 December 2011, to the best of my knowledge and belief, there have been no contraventions of the auditor independence requirements of the *Corporations Act 2001* or any applicable code of professional conduct.



Ernst & Young



Joanne Lonergan  
Partner  
30 March 2012

**DIRECTORS' DECLARATION**

In accordance with a resolution of the directors of Melbourne IT Ltd, I state that:

- (1) In the opinion of the directors:
- (a) the financial statements and notes of Melbourne IT Ltd for the financial year ended 31 December 2011 are in accordance with the Corporations Act 2001, including:
- (i) giving a true and fair view of its financial position as at 31 December 2011 and of its performance for the year ended on that date; and
  - (ii) complying with Accounting Standards (including the Australian Accounting Interpretations) and Corporations Regulations 2001; and
- (b) the financial statements and notes also comply with International Financial Reporting Standards as disclosed in note 1(a).
- (c) there are reasonable grounds to believe that the company will be able to pay its debts as and when they become due and payable.
- (2) This declaration has been made after receiving the declarations required to be made to the directors in accordance with section 295A of the Corporations Act 2001 for the financial year ended 31 December 2011.
- (3) In the opinion of the directors, as at the date of this declaration, there are reasonable grounds to believe that the members of the Closed Group, as identified in note 36, as parties to a Deed of Cross Guarantee, will be able to meet any obligations or liabilities to which they are, or may become subject to, under the deed as described in note 36.

On behalf of the Board



Simon Jones (Chairman)

Melbourne, 30 March 2012



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## Independent audit report to the members of Melbourne IT Limited

### Report on the Financial Report

We have audited the accompanying financial report of Melbourne IT Limited which comprises the consolidated statement of financial position as at 31 December 2011, the consolidated statement of comprehensive income, consolidated statement of changes in equity and the consolidated statement of cash flows for the year then ended, notes comprising a summary of significant accounting policies and other explanatory information, and the directors' declaration of the consolidated entity comprising the company and the entities it controlled at the year's end or from time to time during the financial year.

### Directors' Responsibility for the Financial Report

The directors of the company are responsible for the preparation of the financial report that gives a true and fair view in accordance with Australian Accounting Standards and the *Corporations Act 2001* and for such internal controls as the directors determine are necessary to enable the preparation of the financial report that is free from material misstatement, whether due to fraud or error. In Note 1 (a), the directors also state, in accordance with Accounting Standard AASB 101 *Presentation of Financial Statements*, that the financial statements comply with International Financial Reporting Standards.

### Auditor's Responsibility

Our responsibility is to express an opinion on the financial report based on our audit. We conducted our audit in accordance with Australian Auditing Standards. Those Auditing Standards require that we comply with relevant ethical requirements relating to audit engagements and plan and perform the audit to obtain reasonable assurance whether the financial report is free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial report. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial report, whether due to fraud or error. In making those risk assessments, the auditor considers internal controls relevant to the entity's preparation and fair presentation of the financial report in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal controls. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the directors, as well as evaluating the overall presentation of the financial report.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

### Independence

In conducting our audit we have met the independence requirements of the *Corporations Act 2001*. We have given to the directors of the company a written Auditor's Independence Declaration, a copy of which is included in the directors' report.

Liability limited by a scheme approved  
under Professional Standards Legislation



### Opinion

In our opinion:

- a. the financial report of Melbourne IT Limited is in accordance with the *Corporations Act 2001*, including:
  - i giving a true and fair view of the consolidated entity's financial position as at 31 December 2011 and of its performance for the year ended on that date; and
  - ii complying with Australian Accounting Standards and the *Corporations Regulations 2001*; and
- b. the financial report also complies with International Financial Reporting Standards as disclosed in Note 1 (a).

### Report on the Remuneration Report

We have audited the Remuneration Report included in the directors' report for the year ended 31 December 2011. The directors of the company are responsible for the preparation and presentation of the Remuneration Report in accordance with section 300A of the *Corporations Act 2001*. Our responsibility is to express an opinion on the Remuneration Report, based on our audit conducted in accordance with Australian Auditing Standards.

### Auditor's Opinion

In our opinion the Remuneration Report of Melbourne IT Limited for the year ended 31 December 2011 complies with section 300A of the *Corporations Act 2001*.

Ernst & Young

Joanne Lonergan  
Partner  
Melbourne  
30 March 2012

### CONSOLIDATED STATEMENT OF FINANCIAL POSITION AS AT 31 DECEMBER 2011

|  | Notes | CONSOLIDATED   |                |
|--|-------|----------------|----------------|
|  |       | 2011<br>\$'000 | 2010<br>\$'000 |
| <b>ASSETS</b>                              |       |                |                |
| <b>Current Assets</b>                      |       |                |                |
| Cash and cash equivalents                  | 22(b) | 19,047         | 23,379         |
| Trade and other receivables                | 8     | 29,244         | 24,890         |
| Inventories                                | 9     | 463            | 562            |
| Prepayment of domain name registry charges |       | 11,465         | 13,317         |
| Derivative financial instruments           | 26    | 14             | 258            |
| Other assets                               | 10    | 3,847          | 2,813          |
| <b>Total Current Assets</b>                |       | <b>64,080</b>  | <b>65,219</b>  |
| <b>Non-Current Assets</b>                  |       |                |                |
| Plant and equipment                        | 11    | 5,360          | 7,665          |
| Intangible assets                          | 12    | 130,661        | 126,641        |
| Deferred income tax assets                 | 13    | 6,536          | 5,971          |
| Prepayment of domain name registry charges |       | 6,534          | 7,609          |
| Other assets                               | 14    | 58             | 43             |
| <b>Total Non-Current Assets</b>            |       | <b>149,149</b> | <b>147,929</b> |
| <b>TOTAL ASSETS</b>                        |       | <b>213,229</b> | <b>213,148</b> |
| <b>LIABILITIES</b>                         |       |                |                |
| <b>Current Liabilities</b>                 |       |                |                |
| Trade and other payables                   | 15    | 21,042         | 14,532         |
| Interest-bearing loans and borrowings      | 16    | 5,896          | 5,904          |
| Provisions                                 | 17    | 4,568          | 4,165          |
| Current tax liabilities                    | 18    | 568            | 904            |
| Income received in advance                 |       | 33,093         | 37,299         |
| <b>Total Current Liabilities</b>           |       | <b>65,167</b>  | <b>62,804</b>  |
| <b>Non-Current Liabilities</b>             |       |                |                |
| Interest-bearing loans and borrowings      | 16    | 34,395         | 40,342         |
| Deferred income tax liability              | 19    | 4,226          | 2,194          |
| Provisions                                 | 20    | 815            | 716            |
| Income received in advance                 |       | 13,957         | 15,226         |
| Derivative financial instruments           | 26    | 439            | 597            |
| <b>Total Non-Current Liabilities</b>       |       | <b>53,832</b>  | <b>59,075</b>  |
| <b>TOTAL LIABILITIES</b>                   |       | <b>118,999</b> | <b>121,879</b> |
| <b>NET ASSETS</b>                          |       | <b>94,230</b>  | <b>91,269</b>  |
| <b>EQUITY</b>                              |       |                |                |
| Contributed equity                         | 21(a) | 66,900         | 64,839         |
| Foreign currency translation reserve       |       | (9,892)        | (9,270)        |
| Options reserve                            |       | 4,166          | 3,880          |
| Hedging reserve                            |       | (127)          | 111            |
| Retained earnings                          |       | 33,183         | 31,709         |
| <b>TOTAL EQUITY</b>                        |       | <b>94,230</b>  | <b>91,269</b>  |

The above consolidated statement of financial position should be read in conjunction with the accompanying notes.

**CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME  
AS AT 31 DECEMBER 2011**

|  |                | CONSOLIDATED   |                |
|--|----------------|----------------|----------------|
| Notes  | 2011<br>\$'000 | 2010<br>\$'000 |                |
|  |                |                |                |
| Revenue  | 4(a)           | 179,768        | 189,793        |
| Other Income   | 4(b)           | 10             | 69             |
| Registry, Hosting and Sundry Other Product Costs                 |                | (62,327)       | (73,435)       |
| <b>Gross profit</b>  |                | <u>117,451</u> | <u>116,427</u> |
| Salaries and employee benefits expenses                          |                | (71,264)       | (68,706)       |
| Depreciation and amortisation expenses                           | 5(a)           | (4,854)        | (6,169)        |
| Amortisation of identifiable intangible assets                   | 5(b)           | (1,271)        | (1,200)        |
| Finance costs  | 5(d)           | (958)          | (1,254)        |
| Other expenses   | 5(c)           | (21,195)       | (19,018)       |
| Share of net (loss) of an associate                              |                | -              | (20)           |
| <b>Profit before tax</b>   |                | <u>17,909</u>  | <u>20,060</u>  |
| Income tax expense   | 6              | (4,385)        | (4,000)        |
| <b>Net profit attributable to members of Melbourne IT Ltd</b>    |                | <u>13,524</u>  | <u>16,060</u>  |
| <b>Other comprehensive income</b>                                |                |                |                |
| Currency translation differences                                 |                | (622)          | (3,370)        |
| Net gains/(losses) on cashflow hedges (net of tax)               |                | (238)          | 42             |
| <b>Other comprehensive income for the period, net of tax</b>     |                | <u>(860)</u>   | <u>(3,328)</u> |
| <b>TOTAL COMPREHENSIVE INCOME FOR THE PERIOD</b>                 |                | <u>12,664</u>  | <u>12,732</u>  |
| Profit attributable to members of the parent                     |                | <u>13,524</u>  | <u>16,060</u>  |
| Total comprehensive income attributable to members of the parent |                | <u>12,664</u>  | <u>12,732</u>  |
| <b>EARNINGS PER SHARE</b>  |                | <b>2011</b>    | <b>2010</b>    |
| Basic earnings per share   | 29             | 16.77 cents    | 20.21 cents    |
| Diluted earnings per share                                       | 29             | 16.60 cents    | 20.20 cents    |

The above consolidated statement of comprehensive income should be read in conjunction with the accompanying notes.

**CONSOLIDATED STATEMENT OF CHANGES IN EQUITY  
FOR THE YEAR ENDED 31 DECEMBER 2011**

|  | FOREIGN<br>CURRENCY<br>RESERVE<br>\$'000 | OPTIONS<br>RESERVE<br>\$'000 | HEDGING<br>RESERVE<br>\$'000 | CONTRIBUTED<br>EQUITY<br>\$'000 | RETAINED<br>EARNINGS<br>\$'000 | TOTAL<br>\$'000 |
|--|--|------------------------------|------------------------------|---------------------------------|--------------------------------|-----------------|
| <b>As at 1 January 2011</b>                                  | (9,270)                                  | 3,880                        | 111                          | 64,839                          | 31,709                         | 91,269          |
| Profit for the period  | -  | -                            | -                            | -                               | 13,524                         | 13,524          |
| Other comprehensive income                                   | (622)                                    | -                            | (238)                        | -                               | -                              | (860)           |
| <b>Total comprehensive income for the period</b>             | (622)                                    | -                            | (238)                        | -                               | 13,524                         | 12,664          |
| <b>Transactions with owners in their capacity as owners:</b> |  |                              |                              |                                 |                                |                 |
| Share based payment  | -  | 286                          | -                            | -                               | -                              | 286             |
| Dividend reinvestment plan                                   | -  | -                            | -                            | 1,906                           | (1,906)                        | -               |
| Exercise of options  | -  | -                            | -                            | 155                             | -                              | 155             |
| Equity dividends   | -  | -                            | -                            | -                               | (10,144)                       | (10,144)        |
| <b>As at 31 December 2011</b>                                | <u>(9,892)</u>                           | <u>4,166</u>                 | <u>(127)</u>                 | <u>66,900</u>                   | <u>33,183</u>                  | <u>94,230</u>   |
| <b>As at 1 January 2010</b>                                  | (5,900)                                  | 3,095                        | 69                           | 63,005                          | 27,539                         | 87,808          |
| Profit for the period  | -  | -                            | -                            | -                               | 16,060                         | 16,060          |
| Other comprehensive income                                   | (3,370)                                  | -                            | 42                           | -                               | -                              | (3,328)         |
| <b>Total comprehensive income for the period</b>             | (3,370)                                  | -                            | 42                           | -                               | 16,060                         | 12,732          |
| <b>Transactions with owners in their capacity as owners:</b> |  |                              |                              |                                 |                                |                 |
| Share based payment  | -  | 785                          | -                            | -                               | -                              | 785             |
| Dividend reinvestment plan                                   | -  | -                            | -                            | 1,622                           | (1,622)                        | -               |
| Exercise of options  | -  | -                            | -                            | 212                             | -                              | 212             |
| Equity dividends   | -  | -                            | -                            | -                               | (10,268)                       | (10,268)        |
| <b>As at 31 December 2010</b>                                | <u>(9,270)</u>                           | <u>3,880</u>                 | <u>111</u>                   | <u>64,839</u>                   | <u>31,709</u>                  | <u>91,269</u>   |

The above consolidated statement of changes in equity should be read in conjunction with the accompanying notes.

**CONSOLIDATED STATEMENT OF CASH FLOWS  
FOR THE YEAR ENDED 31 DECEMBER 2011**

|  | Notes | CONSOLIDATED    |                 |
|--|-------|-----------------|-----------------|
|  |       | 2011<br>\$'000  | 2010<br>\$'000  |
| <b>CASH FLOWS FROM OPERATING ACTIVITIES</b>                  |       |                 |                 |
| Receipt of service revenue and recoveries (inclusive of GST) |       | 192,108         | 203,717         |
| Payments to suppliers and employees (inclusive of GST)       |       | (168,016)       | (177,524)       |
| Interest received  |       | 422             | 631             |
| Interest paid  |       | (1,424)         | (1,753)         |
| Bank charges and credit card merchant fees                   |       | (958)           | (1,254)         |
| Income tax paid  |       | (3,033)         | (5,088)         |
| <b>NET CASH FLOWS FROM OPERATING ACTIVITIES</b>              | 22(a) | <b>19,099</b>   | <b>18,729</b>   |
| <b>CASH FLOWS FROM INVESTING ACTIVITIES</b>                  |       |                 |                 |
| Purchase of plant and equipment and intangible assets        |       | (2,759)         | (5,033)         |
| Capitalisation of intangible expenditure                     |       | (5,488)         | (5,500)         |
| Proceeds on sale of plant and equipment                      |       | 256             | 1,474           |
| Receipt of deposits to be transferred to ICANN               |       | 742             | 0               |
| Investment in joint venture - Advantate Pty Ltd              |       | -               | (20)            |
| <b>NET CASH FLOWS USED IN INVESTING ACTIVITIES</b>           |       | <b>(7,249)</b>  | <b>(9,079)</b>  |
| <b>CASH FLOWS FROM FINANCING ACTIVITIES</b>                  |       |                 |                 |
| Repayment of interest bearing liabilities                    |       | (5,934)         | (5,337)         |
| Proceeds from issue of ordinary shares - ESOP                |       | 155             | 212             |
| Payment of dividend on ordinary shares                       |       | (10,144)        | (10,268)        |
| <b>NET CASH FLOWS USED IN FINANCING ACTIVITIES</b>           |       | <b>(15,923)</b> | <b>(15,393)</b> |
| <b>NET DECREASE IN CASH AND CASH EQUIVALENTS</b>             |       | <b>(4,073)</b>  | <b>(5,743)</b>  |
| Net foreign exchange differences                             |       | (259)           | (1,255)         |
| Cash and cash equivalents at beginning of period             |       | 23,379          | 30,377          |
| <b>CASH AND CASH EQUIVALENTS AT END OF PERIOD</b>            | 22(b) | <b>19,047</b>   | <b>23,379</b>   |

The above statement of cash flows should be read in conjunction with the accompanying notes.

**NOTES TO THE FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 31 DECEMBER 2011**
**CORPORATE INFORMATION**

The financial report of Melbourne IT Ltd for the year ended 31 December 2011 was authorised for issue in accordance with a resolution of the directors on 22 March 2012.

Melbourne IT Ltd is a company limited by shares incorporated and domiciled in Australia whose shares are publicly traded on the Australian Stock Exchange.

The nature of the operations and principal activities of the Group are described in Notes 1(e).

**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**
**Basis of Preparation**

The financial report is a general-purpose financial report, which has been prepared in accordance with the requirements of the Corporations Act 2001, Australian Accounting Standards, and other authoritative pronouncements of the Australian Accounting Standards Board.

The financial report has been prepared on a historical cost basis, except for derivative financial instruments that have been measured at fair value. The carrying values of recognised assets and liabilities that are hedged with fair value hedges are adjusted to record changes in the fair values attributable to the risks that are being hedged.

The financial report is presented in Australian dollars and all values are rounded to the nearest thousand dollars (\$'000), unless otherwise stated, under the option available to the company under ASIC Class Order 98/0100. The company is an entity to which the class order applies.

**(a) Compliance with IFRS**

The financial report complies with Australian Accounting Standards and International Financial Reporting Standards ('IFRS') as issued by the International Accounting Standards Board.

**(b) New Accounting Standards and Interpretations**
*(i) Changes in accounting policy and disclosures*

The accounting policies adopted are consistent with those of the previous financial year except as follows:

The Group has adopted the following new and amended Australian Accounting Standards and AASB Interpretations as of 1 January 2011.

- AASB 124 Related Party Disclosures (amendment) effective 1 January 2011
- AASB 132 Financial Instruments: Presentation (amendment) effective 1 February 2010

**Annual Improvements Project**

In May 2010, the AASB issued its third omnibus of amendments to its standards, primarily with a view to removing inconsistencies and clarifying wording. There are separate transitional provisions for each standard. The adoption of the following amendments resulted in changes to accounting policies, but did not have any impact on the financial position or performance of the Group:

- AASB 3 Business Combinations: The measurement options available for non-controlling interest (NCI) were amended. Only components of NCI that constitute a present ownership interest that entitles their holder to a proportionate share of the entity's net assets in the event of liquidation should be measured at either fair value or at the present ownership instruments' proportionate share of the acquiree's identifiable net assets. All other components are to be measured at their acquisition date fair value (see Note 23). The amendments to AASB 3 are effective for annual periods beginning on or after 1 July 2011.
- AASB 7 Financial Instruments — Disclosures: The amendment was intended to simplify the disclosures provided by reducing the volume of disclosures around collateral held and improving disclosures by requiring qualitative information to put the quantitative information in context. The Group reflects the revised disclosure requirements in Note 26.
- AASB 101 Presentation of Financial Statements: The amendment clarifies that an entity may present an analysis of each component of other comprehensive income maybe either in the statement of changes in equity or in the notes to the financial statements.

**NOTES TO THE FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 31 DECEMBER 2011**

**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

(i) *Changes in accounting policy and disclosure (Continued)*

Other amendments resulting from the Annual Improvements Project to the following Standards did not have any impact on the accounting policies, financial position or performance of the Group:

- AASB 3 Business Combinations (Contingent consideration arising from business combination prior to adoption of AASB 3 (as revised in 2008))
- AASB 3 Business Combinations (Un-replaced and voluntarily replaced share-based payment awards)
- AASB 127 Consolidated and Separate Financial Statements
- AASB 134 Interim Financial Statements

(ii) *Accounting Standards and Interpretations issued but not yet effective*

Australian Accounting Standards that have recently been issued or amended but which are not yet effective and have not been adopted by the Group for the annual reporting period ended 31 December 2011 are outlined in the table below.

| Reference   | Title  | Summary   | Application Date of Standard* | Impact on Group Financial Report  | Application Date for Group* |
|-------------|--|---|-------------------------------|---|-----------------------------|
| AASB 1054   | Australian Additional Disclosures  | This standard is as a consequence of phase 1 of the joint Trans-Tasman Convergence project of the AASB and FRSB. This standard, with AASB 2011-1 relocates all Australian specific disclosures from other standards to one place and revises disclosures in the following areas:<br>(a) Compliance with Australian Accounting Standards<br>(b) The statutory basis or reporting framework for financial statements<br>(c) Whether the financial statements are general purpose or special purpose<br>(d) Audit fees<br>(e) Imputation credits | 1-Jul-11                      | The amendments to the Accounting Standard are not expected to have a material impact on the Group's financial position or performance.  | 1-Jan-12                    |
| AASB 2011-9 | Amendments to Australian Accounting Standards – Presentation of Other Comprehensive Income [AASB 101]                          | This standard requires entities to group items presented in other comprehensive income on the basis of whether they are potentially reclassifiable to profit or loss subsequently (reclassification adjustments).   | 1-Jul-12                      | The amendments to the Accounting Standard relate only to disclosure requirements so will not materially impact the Group's financial position or performance.   | 1-Jan-13                    |
| AASB 2011-4 | Amendments to Australian Accounting Standards to Remove Individual Key Management Personnel Disclosure Requirements [AASB 124] | This standard makes amendments to remove individual key management personnel disclosure requirements from AASB 124.   | 1-Jul-13                      | The amendments to the Accounting Standard relate only to disclosure requirements so will not materially impact the Group's financial position or performance.   | 1-Jan-14                    |
| AASB 119    | Employee Benefits  | The definition of short-term benefits has been revised, meaning some annual leave entitlements may become long-term in nature with a revised measurement. Similarly the timing for recognising a provision for termination benefits has been revised, such that provisions can only be recognised when the offer cannot be withdrawn. Consequential amendments were also made to other standards via AASB 2011-10.  | 1-Jan-13                      | Whilst the impact of the application of the new Standard is currently being assessed, our initial assessment is that there should be no material impact on the Group's financial position or performance. | 1-Jan-13                    |
| AASB 12     | Disclosure of Interests in Other Entities  | AASB 12 includes all disclosures relating to an entity's interests in subsidiaries, joint arrangements, associates and structured entities. New disclosures have been introduced about the judgements made by management to determine whether control exists, and to require summarised information about joint arrangements, associates and structured entities and subsidiaries with non-controlling interests.   | 1-Jan-13                      | The amendments to the Accounting Standard relate only to disclosure requirements so will not materially impact the Group's financial position or performance.   | 1-Jan-13                    |

**NOTES TO THE FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 31 DECEMBER 2011**

**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

(ii) *Accounting Standards and Interpretations issued but not yet effective (continued)*

| Reference | Title                             | Summary  | Application Date of Standard* | Impact on Group Financial Report   | Application Date for Group* |
|-----------|-----------------------------------|--|-------------------------------|--|-----------------------------|
| AASB 9    | Financial Instruments             | AASB 9 includes requirements for the classification and measurement of financial assets. It was further amended by AASB 2010-7 to reflect amendments to the accounting for financial liabilities. These requirements improve and simplify the approach for classification and measurement of financial assets compared with the requirements of AASB 139. The main changes are described below.<br>(a) Financial assets that are debt instruments will be classified based on (1) the objective of the entity's business model for managing the financial assets; (2) the characteristics of the contractual cash flows.<br>(b) Allows an irrevocable election on initial recognition to present gains and losses on investments in equity instruments that are not held for trading in other comprehensive income. Dividends in respect of these investments that are a return on investment can be recognised in profit or loss and there is no impairment or recycling on disposal of the instrument.<br>(c) Financial assets can be designated and measured at fair value through profit or loss at initial recognition if doing so eliminates or significantly reduces a measurement or recognition inconsistency that would arise from measuring assets or liabilities, or recognising the gains and losses on them, on different bases.<br>(d) Where the fair value option is used for financial liabilities the change in fair value is to be accounted for as follows:<br>•The change attributable to changes in credit risk are presented in other comprehensive income (OCI)<br>•The remaining change is presented in profit or loss<br>Consequential amendments were also made to other standards as a result of AASB 9, introduced by AASB 2009-11. | 1-Jan-13                      | Whilst the impact of the application of the new Standard is currently being assessed on the foreign exchange contracts and interest rate swap, our initial assessment is that there should be no material impact on the Group's financial position or performance. | 1-Jan-13                    |
| AASB 10   | Consolidated Financial Statements | AASB 10 establishes a new control model that applies to all entities. It replaces parts of AASB 127 Consolidated and Separate Financial Statements dealing with the accounting for consolidated financial statements and UIG-112 Consolidation – Special Purpose Entities. The new control model broadens the situations when an entity is considered to be controlled by another entity and includes new guidance for applying the model to specific situations, including when acting as a manager may give control, the impact of potential voting rights and when holding less than a majority voting rights may give control. This is likely to lead to more entities being consolidated into the group. Consequential amendments were also made to other standards via AASB 2011-7 and amendments to AASB 127.   | 1-Jan-13                      | The amendments to the Accounting Standard are not expected to have a material impact on the Group's financial position or performance.   | 1-Jan-13                    |

\* Application date is for the reporting periods beginning on or after the date shown in the above table



**NOTES TO THE FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 31 DECEMBER 2011**

**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

**(c) Basis of Consolidation**

The consolidated financial statements comprise the financial statements of Melbourne IT Ltd and its subsidiaries as at 31 December each year ('the Group'). Subsidiaries are all those entities over which the Group has the power to govern the financial and operating policies so as to obtain benefits from their activities.

The financial statements of subsidiaries are prepared for the same reporting period as the parent company, using consistent accounting policies. In preparing the consolidated financial statements, all intercompany balances and transactions, including unrealised profits arising from intra-group transactions, have been eliminated in full.

Subsidiaries are fully consolidated from the date on which control is transferred to Melbourne IT Ltd and cease to be consolidated from the date on which control is transferred out of Melbourne IT Ltd.

Investments in subsidiaries held by Melbourne IT Ltd are accounted for at cost, where no fair value hedge is in place, in the separate financial statements of the parent entity, net of any impairment charges. Dividends received from subsidiaries are recorded as a component of other revenues in the separate income statement of the parent entity, and do not impact the recorded cost of the investment. Upon receipt of dividend payments from subsidiaries, the parent will assess whether any indicators of impairment of the carrying value of the investment in the subsidiary exist. Where such indicators exist, to the extent that the carrying value of the investment exceeds its recoverable amount, an impairment loss is recognised.

The acquisition of subsidiaries is accounted for using the acquisition method of accounting. The acquisition method of accounting involves recognising at acquisition date, separately from goodwill, the identifiable assets acquired, the liabilities assumed and any non-controlling interest in the acquiree. The identifiable assets acquired and the liabilities assumed are measured at their acquisition date fair values. The difference between the above items and the fair value of the consideration (including the fair value of any pre-existing investment in the acquiree) is goodwill or a discount on acquisition.

After initial recognition, goodwill is measured at cost less any accumulated impairment losses. For the purpose of impairment testing, goodwill acquired in a business combination is, from the acquisition date, allocated to each of the Group's cash-generating units that are expected to benefit from the combination, irrespective of whether other assets or liabilities of the acquirer are assigned to those units. Where goodwill forms part of a cash-generating unit and part of the operation within that unit is disposed of, the goodwill associated with the operation disposed of is included in the carrying amount of the operation when determining the gain or loss on disposal of the operation. Goodwill disposed of in this circumstance is measured based on the relative values of the operation disposed of and the portion of the cash-generating unit retained.

Where a fair value hedge is in place, the subsidiaries are restated at fair value at period end in line with AASB 139 in the separate financial statements for the parent entity.

Where there is loss of control of a subsidiary, the consolidated financial statements include the results for the part of the reporting period during which Melbourne IT Ltd has control. A change in the ownership interest of a subsidiary that does not result in a loss of control, is accounted for as an equity transaction.

**(d) Business Combinations**

**Subsequent to 1 January 2010**

Business combinations are accounted for using the acquisition method. The consideration transferred in a business combination shall be measured at fair value, which shall be calculated as the sum of the acquisition date fair values of the assets transferred by the acquirer, the liabilities incurred by the acquirer to former owners of the acquiree and the equity issued by the acquirer, and the amount of any non-controlling interest in the acquiree. For each business combination, the acquirer measures the non-controlling interest in the acquiree either at fair value or at the proportionate share of the acquiree's identifiable net assets. Acquisition-related costs are expensed as incurred, and included in other expenses.

When the Group acquires a business, it assesses the financial assets and liabilities assumed for appropriate classification and designation in accordance with the contractual terms, economic conditions, the Group's operating or accounting policies and other pertinent conditions as at the acquisition date. This includes the separation of embedded derivatives in host contracts by the acquiree.

If the business combination is achieved in stages, the acquisition date fair value of the acquirer's previously held equity interest in the acquiree is remeasured to fair value at the acquisition date through profit or loss.

Any contingent consideration to be transferred by the acquirer will be recognised at fair value at the acquisition date. Subsequent changes to the fair value of the contingent consideration which is deemed to be an asset or liability will be recognised in accordance with AASB 139 either in profit or loss or as a change to other comprehensive income. If the contingent consideration is classified as equity, it should not be remeasured until it is finally settled within equity.

**Prior to 1 January 2010**

In comparison to the above-mentioned requirements, the following difference applied: Business combinations were accounted for using the purchase method. Transaction costs directly attributable to the acquisition formed part of the acquisition costs. Contingent consideration was recognised if, and only if, the Group had a present obligation, the economic outflow was more likely than not and a reliable estimate was determinable. Subsequent adjustments to the contingent consideration were adjusted against goodwill.

**NOTES TO THE FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 31 DECEMBER 2011**

**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

**(e) Operating Segment**

An operating segment is a component of an entity that engages in business activities from which it may earn revenues and incur expenses, whose operating results are regularly reviewed by the entity's chief operating decision maker to make decisions about resources to be allocated to the segment and assess its performance and for which discrete financial information is available.

Executive management meet on a monthly basis to assess the performance of each segment by analysing the segment's earnings before interest and tax (EBIT).

Transfer prices between operating segments are set on an arms' length basis in a manner similar to transactions with third parties. Segment revenue, expense and segment result include transfers between business segments. Those transfers are eliminated on consolidation.

Consistent with the requirements of AASB 8, as the Chief Operating Decision Maker does not receive information regarding segment assets, no disclosure of segment assets has been provided.

*Accounting policies and inter segment transactions*

The accounting policies used by the group in reporting segments internally are the same as those contained in note 1.

*Identification of reportable segments*

Operating segments have been identified based on the information provided to the Chief Operating Decision Maker, being the CEO.

The operating segments are identified by Management based on the manner in which the product is sold, whether retail or wholesale, and the nature of the services provided, the identity of the service line manager and country of origin. Discrete financial information about each of these operating businesses is reported to the executive management team on at least a monthly basis.

Where operating segments meet the aggregation criteria, these are aggregated into reported segments. The Group's reportable segments are:

**SMB eBusiness Solutions ("SMB") - formerly Business and Consumer**

This Division has a focus on the Australian and New Zealand markets developing integrated online solutions for the fast-growing SME (Small to Medium Enterprise) and SOHO (Small Office and Home Office) sectors. These solutions include domain forwarding, web hosting, search engine optimisation and web site development.

**Global Partner Solutions ("GPS") - formerly Reseller**

Melbourne IT supplies a technical and support solution for domain name registration and other online business services to a global network of reseller clients. Resellers are given access to Melbourne IT's domain name registration, shared hosting and maintenance systems. Benefits to reseller clients include application of a real time automated system that can be integrated into the Reseller website, together with access to specialist support and account management services.

**Digital Brand Services ("DBS")**

The Digital Brand Services Division's core business is online brand protection including the management of domain name portfolios. Strategically, DBS services are aimed at protecting and maximising the value of brands online.

**Enterprise Services ("ES") - formerly Corporate and Government**

The Enterprise Services Division provides business grade web application hosting services, as well as mission control hosting services to corporate and government clients throughout Australasia.

**For The Record ("FTR")**

For The Record is a supplier of rich media content management systems for courtrooms, hearing rooms, public meeting venues and law enforcement.

**NOTES TO THE FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 31 DECEMBER 2011**

**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

**(f) Foreign Currency Transactions**

Both the functional and presentation currency of Melbourne IT Ltd and its Australian subsidiaries is Australian dollars (A\$).

Transactions in foreign currencies are initially recorded in the functional currency at the exchange rates ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated at the rate of exchange ruling at the reporting date. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rate as at the date of the initial transaction.

The functional currency of each overseas subsidiary is as follows:

|  |                              |
|--|------------------------------|
| • Investment in Spanish, French, German and Dutch subsidiaries | - Euro                       |
| • Investment in Swedish subsidiaries                           | - SEK (Swedish Krona)        |
| • Investment in New Zealand subsidiary                         | - NZD (New Zealand Dollar)   |
| • Investment in US subsidiaries                                | - USD (United States Dollar) |
| • Investment in UK subsidiaries                                | - GBP (Great British Pound)  |
| • Investment in Danish subsidiaries                            | - DKK (Danish Krone)         |
| • Investment in South African subsidiary                       | - ZAR (South African Rand)   |
| • Investment in Hong Kong subsidiary                           | - HKD (Hong Kong Dollar)     |
| • Investment in Norwegian subsidiary                           | - NOK (Norwegian Krone)      |

The assets and liabilities of these overseas subsidiaries are translated into the presentation currency of Melbourne IT Ltd at the rate of exchange ruling at the reporting date and the statement of comprehensive income is translated at the weighted average exchange rates for the period.

The exchange differences arising on the retranslation are taken directly to other comprehensive income. On disposal of a foreign entity, the deferred cumulative amount recognised in other comprehensive income relating to that particular foreign operation is recognised in the determination of profit and loss for the year.

On consolidation, exchange differences arising from the translation of any net investment in foreign entities, and of borrowings and other financial instruments designed as hedges of such investments are taken to the foreign currency translation reserve in equity. When a foreign operation is sold or any borrowings forming part of the net investment are repaid, a proportionate share of such exchange differences are recognised in the Statement of Comprehensive Income, as part of the gain on sale or loss on sale where applicable.

**(g) Cash and Cash Equivalents**

Cash and short-term deposits in the statement of financial position comprise cash at bank and on hand and short-term deposits with an original maturity of three months or less.

For the purposes of the statement of cash flows, cash and cash equivalents consist of cash and cash equivalents as defined above.

**(h) Trade and Other Receivables**

Trade receivables, which generally have 14-60 day terms, are recognised and carried at amortised cost which is at original invoice amount less an allowance for any uncollectible amounts. An estimate for doubtful debts is made when collection of the full amount is no longer probable. Bad debts are written off when identified.

**(i) Inventories**

Inventories including raw materials, work in progress and finished goods are valued at the lower of cost and net realisable value.

Costs incurred in bringing each product to its present location and condition are accounted for as follows:

- Raw materials – purchase cost on a first-in, first-out basis. The cost of purchase comprises the purchase price including other costs directly attributable to the acquisition of raw materials.
- Finished goods and work-in-progress – cost of direct materials and labour and a proportion of variable and fixed manufacturing overheads based on normal operating capacity. Costs are assigned on the basis of weighted average costs.

Net realisable value is the estimated selling price in the ordinary course of business, less estimated costs of completion and the estimated costs necessary to make the sale.

**(j) Expenditure Carried Forward - Prepayment of Domain Name Registry Charges**

Significant items of expenditure having a benefit or relationship to more than one period are written off over the periods to which such expenditure relates.

**NOTES TO THE FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 31 DECEMBER 2011**

**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

**(k) Derivative Financial Instruments**

Melbourne IT Ltd conducts a substantial amount of its business in US dollars ("USD") and is therefore exposed to movements in the AUD / USD dollar exchange rate. The company actively manages this risk via its foreign currency risk management strategy.

As at 31 December 2011, Melbourne IT Ltd has entered into a number of foreign currency option contracts ('derivative financial instruments') with the primary objective of minimising the impact of currency fluctuations on the company. The strategy provides more certainty over earned USD sales transactions.

The Group has also entered into an interest rate swap agreement with the primary objective of minimising the impact of interest rate fluctuations on the company. The strategy provides more certainty over the interest rate charged on the US Dollar loan.

Melbourne IT Ltd uses derivative financial instruments, such as foreign exchange options, interest rate swaps to hedge its risks associated with currency and interest rate fluctuations. Such derivative financial instruments are stated at fair value. The fair value of forward exchange contracts is calculated by reference to current forward exchange rates for contracts with similar maturity profiles.

For the purposes of hedge accounting, hedges are classified as cash flow hedges where they hedge exposure to variability in cash flows that is either attributable to a particular risk associated with a recognised asset or liability or a forecasted transaction.

In relation to cash flow hedges (forward foreign currency contracts) to hedge firm commitments which meet the conditions for special hedge accounting, the portion of the gain or loss on the hedging instrument that is determined to be an effective hedge is recognised directly in other comprehensive income and the ineffective portion is recognised in the determination of profit and loss for year.

When the hedged firm commitment results in the recognition of an asset or a liability, then, at the time the asset or liability is recognised, the associated gains or losses that had previously been recognised in other comprehensive income are included in the initial measurement of the acquisition cost or other carrying amount of the asset or liability.

For all other cash flow hedges, the gains or losses that are recognised in other comprehensive income are transferred to profit and loss in the same year in which the hedged firm commitment affects the net profit and loss, for example when the future sale actually occurs.

For derivatives that do not qualify for hedge accounting, any gains or losses arising from changes in fair value are taken directly to profit and loss.

Hedge accounting is discontinued when the hedging instrument expires or is sold, terminated or exercised, or no longer qualifies for hedge accounting. At that point in time, any cumulative gain or loss on the hedging instrument recognised in other comprehensive income is kept in equity until the forecasted transaction occurs. If a hedged transaction is no longer expected to occur, the net cumulative gain or loss recognised in equity is transferred to profit and loss.

**(l) Plant and Equipment**

Plant and equipment is stated at cost less accumulated depreciation and any impairment in value.

*Depreciation*

Depreciation is provided on a straight-line or diminishing value basis on all plant and equipment. Major depreciation periods are:-

|                        | <b>2011</b>    | <b>2010</b>    |
|------------------------|----------------|----------------|
| Leasehold improvements | The lease term | The lease term |
| Plant and equipment    | 2 to 4 years   | 2 to 4 years   |
| Furniture and Fittings | 2 to 5 years   | 2 to 5 years   |

*Impairment*

The carrying values of plant and equipment are reviewed for impairment when events or changes in circumstances indicate the carrying value may not be recoverable. For an asset that does not generate largely independent cash inflows, the recoverable amount is determined for the cash-generating unit to which the asset belongs. If any such indication exists and where the carrying values exceed the estimated recoverable amount, the assets or cash-generating units are written down to their recoverable amount.

**NOTES TO THE FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 31 DECEMBER 2011**

**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

**(m) Recoverable Amount of Assets**

At each reporting date, Melbourne IT Ltd assesses whether there is any indication that an asset may be impaired. Where an indicator of impairment exists, Melbourne IT Ltd makes a formal estimate of recoverable amount. Where the carrying amount of an asset exceeds its recoverable amount the asset is considered impaired and is written down to its recoverable amount.

Recoverable amount is the greater of fair value less costs to sell and value in use. It is determined for an individual asset, unless the asset's value in use cannot be estimated to be close to its fair value less costs to sell and it does not generate cash inflows that are largely independent of those from other assets or groups of assets, in which case, the recoverable amount is determined for the cash-generating unit to which the asset belongs.

In assessing value in use, the estimated future cash flows are discounted to their present value using a pre tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

**(n) Goodwill**

Goodwill on acquisition is initially measured at cost being the excess of the cost of the business combination over the acquirer's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities.

Following initial recognition, goodwill is measured at cost less any accumulated impairment losses. Goodwill is not amortised. Goodwill is reviewed for impairment, annually or more frequently if events or changes in circumstances indicate that the carrying value may be impaired.

As at the acquisition date, any goodwill acquired is allocated to each of the cash-generating units expected to benefit from the combination's synergies. Impairment is determined by assessing the recoverable amount of the cash-generating unit to which the goodwill relates. Where the recoverable amount of the cash-generating unit is less than the carrying amount, an impairment loss is recognised. Impairment losses recognised for goodwill are not permitted to be subsequently reversed.

**(o) Intangible Assets**

*Acquired both separately and from a business combination*

Intangible assets acquired separately are capitalised at cost and from a business combination are capitalised at fair value as at the date of acquisition. Following initial recognition, the cost model is applied to the class of intangible assets.

Where amortisation is charged on assets with finite lives, this expense is taken to profit and loss through the 'amortisation of identifiable intangible assets' line item.

Gains or losses arising from derecognition of an intangible asset are measured as the difference between the net disposal proceeds and the carrying amount of the asset and are recognised in the profit and loss when the asset is derecognised.

*Internally Generated Assets: Assets Under Construction - Transformation Projects*

As explained in note 12, the Group has commenced a transformation project to develop and implement Integrated Web Services, Oracle Financials and Operational Support Systems. Costs relating to the research phase of the project are expensed while costs relating to the development phase are capitalised as Capitalised Software: Assets Under Construction - Transformation Projects. Once operational they will be amortised over a useful life of 4 years for hardware and 5 years for license, integration and labour costs.

A summary of the policies applied to the Group's intangible assets is as follows:

| <b>Customer Contracts</b>         |  |
|-----------------------------------|--|
| Useful lives                      | Finite   |
| Amortisation                      | Amortised over the estimated churn of the customer base.                           |
| Impairment testing                | Amortisation method reviewed at each financial year-end and when indicators exist. |
| <b>Market Related Intangibles</b> |  |
| Useful lives                      | Indefinite   |
| Amortisation                      | No amortisation.   |
| Impairment testing                | Annually and more frequently when indicator exists.                                |
| <b>Software Platforms</b>         |  |
| Useful lives                      | Finite   |
| Amortisation                      | Amortised over expected useful life of 5 years                                     |
| Impairment testing                | Amortisation method reviewed at each financial year-end and when indicators exist. |

The carrying value of intangible assets denominated in foreign currencies is revalued at the year end spot rate of each reporting period, leading to changes in the carrying value of the intangible assets in reporting currency. Any revaluation amounts are recognised directly in the foreign currency translation reserve.

**NOTES TO THE FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 31 DECEMBER 2011**

**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

**(p) Investments in Subsidiaries**

All investments are initially recognised at cost, being the fair value of the consideration given and including acquisition charges associated with the investment.

**(q) Trade and Other Payables**

Trade and other payables are carried at amortised cost and due to their short term nature they are not discounted. They represent liabilities for goods and services provided to the Group prior to the end of the year that are unpaid and arise when the Group becomes obliged to make future payments in respect of the purchase of these goods and services. The amounts are unsecured and are usually paid within 30 days of recognition.

**(r) Interest-bearing Loans and Borrowings**

All loans and borrowings are initially recognised at the fair value of the consideration received less directly attributable transaction costs. After initial recognition, interest-bearing loans and borrowings are subsequently measured at amortised cost using the effective interest method. Fees paid on the establishment of loan facilities that are yield related are included as part of the carrying amount of the loans and borrowings. Borrowings are classified as current liabilities unless the group has an unconditional right to defer settlement of the liability for a least 12 months after the reporting date.

**(s) Borrowing Costs**

Borrowing costs are recognised as an expense when incurred.

**(t) Provisions**

Provisions are recognised when Melbourne IT Ltd has a present obligation (legal or constructive) as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation.

**(u) Leases**

Finance leases, which transfer to Melbourne IT Ltd substantially all the risks and benefits incidental to ownership of the leased item, are capitalised at the inception of the lease at the fair value of the leased property or, if lower, at the present value of the minimum lease payments.

Lease payments are apportioned between the finance charges and reduction of the lease liability so as to achieve a constant rate of interest on the remaining balance of the liability. Finance charges are charged directly against profit or loss.

Capitalised leased assets are depreciated over the shorter of the estimated useful life of the asset or the lease term. Leases where the lessor retains substantially all the risks and benefits of ownership of the asset are classified as operating leases. Operating lease payments are recognised as an expense in the profit and loss on a straight-line basis over the lease term. Operating lease incentives are recognised as a liability when received and subsequently reduced by allocating lease payments between rental expense and reduction of the liability.

**NOTES TO THE FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 31 DECEMBER 2011**

**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

**(v) Revenue Recognition**

Revenue is recognised to the extent that it is probable that the economic benefits will flow to the entity and the revenue can be reliably measured. The following specific recognition criteria must also be met before revenue is recognised:

**Group**

**Rendering of services - domain names**

Revenue is recognised by reference to percentage of completion method. The percentage of completion is determined by reference to the extent of services performed to date on the agreement as a percentage of total services to be performed under the agreement. Revenue is recognised in the financial period in which services are rendered.

Where cash has been received for services yet to be performed pursuant to the agreement, the amount has been classified in the statement of financial position as "Income received in advance".

**Melbourne IT Ltd and Domainz Ltd**

The following table summarises the domain name registration revenue and registry cost recognition policy for Melbourne IT Ltd and Domainz Ltd:

| Length of Registration - Years | First Month | Per Other Month |
|--------------------------------|-------------|-----------------|
| 1                              | 78.0000%    | 2.0000%         |
| 2                              | 54.0000%    | 2.0000%         |
| 3                              | 36.0000%    | 1.8286%         |
| 4                              | 27.0000%    | 1.5532%         |
| 5                              | 21.6000%    | 1.3288%         |
| 6                              | 18.0000%    | 1.1549%         |
| 7                              | 15.4286%    | 1.0189%         |
| 8                              | 13.5000%    | 0.9105%         |
| 9                              | 12.0000%    | 0.8224%         |
| 10                             | 10.8000%    | 0.7496%         |

**Rendering of services – non domain name revenue**

Non domain name registration revenue is recognised on an earned basis for all entities within the Melbourne IT Ltd Group.

**Sale of goods**

Revenue is recognised when the significant risks and rewards of ownership of the goods have passed to the buyer and the costs incurred in respect of the transaction can be measured reliably. Risks and rewards are considered passed to the buyer at the time of delivery of the goods to the customer.

**Interest**

Revenue is recognised as the interest accrues (using the effective interest method, which is the rate that exactly discounts estimated future cash receipts through the expected life of the financial instrument) to the net carrying amount of the financial asset.

**Dividends**

Revenue is recognised when the shareholders' right to receive the payment is established.

**(w) Employee Entitlements**

Provision is made for employee entitlements accumulated as a result of employees rendering services up to the reporting date. These benefits include wages and salaries, annual leave and long service leave.

Liabilities arising in respect of wages and salaries, annual leave and any other employee entitlements expected to be settled within twelve months of the reporting date are measured at their nominal amounts based on remuneration rates which are expected to be paid when the liability is settled. All other employee entitlement liabilities are measured at the present value of the estimated future cash outflow to be made in respect of services provided by employees up to the reporting date. In determining the present value of future cash outflows, the market yield as at the reporting date on national government bonds, which have terms to maturity approximating the terms of the related liability are used.

Employee entitlement expenses and revenues arising in respect of the following categories:

- wages and salaries, non-monetary benefits, annual leave, long service leave and other entitlements; and
- other types of employee entitlements

are recognised against profits on a net basis in their respective categories.

**NOTES TO THE FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 31 DECEMBER 2011**

**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

**(x) Share-based Payment Transactions**

**(i) Option Plans**

The Melbourne IT Ltd Executive & Employee Option Plans have been established where the managing director and employees of the company are issued with options over the ordinary shares of Melbourne IT Ltd ('equity-settled transactions'). The options, issued for nil consideration, are issued in accordance with performance guidelines established by the directors of Melbourne IT Ltd.

The options cannot be transferred and will not be quoted on the ASX. The managing director and all full-time or permanent part-time employees of the company or any of its related body corporate are eligible to participate in the option plan.

Options are issued free of charge. Each option is to subscribe for one fully paid Share. When issued, the Share will rank equally with other Shares. The options are not transferable except to the legal personal representative of a deceased or legally incapacitated option holder. The options are issued for a term of 5 years.

Under the Option Plans, the options have other terms specified at the time the options are offered. These terms differ between the managing director, senior executives and general employees ('employees'). The terms may include conditions, which set out the number or percentage of options able to be exercised at certain time periods or under certain circumstances. For the managing director and senior executives performance conditions may require that the number of options able to be exercised be reduced or that some or all of the options lapse under specified circumstances.

The Board has adopted certain policies concerning the terms of the options to be granted under the Option Plans. The Board has the absolute discretion to change these policies at any time, although any change in its policies will have an effect only on options that are issued at or after the time of the change. The cost of these equity-settled transactions with employees is measured by reference to the fair value at the date at which they are granted.

The fair value is determined by an external valuer using a binomial model. In valuing equity-settled transactions, no account is taken of any performance conditions, other than conditions linked to the price of the shares of Melbourne IT Ltd ('market conditions').

The cost of equity-settled transactions is recognised, together with a corresponding increase in equity, over the period in which the performance conditions are fulfilled, ending on the date on which the relevant employees become fully entitled to the award ('vesting date').

The cumulative expense recognised for equity-settled transactions at each reporting date until vesting date reflects (i) the extent to which the vesting period has expired and (ii) the number of awards that, in the opinion of the directors of Melbourne IT Ltd, will ultimately vest. This opinion is formed based on the best available information at balance date.

No expense is recognised for awards that do not ultimately vest, except for awards where vesting is conditional upon a market condition.

Where the terms of an equity-settled award are modified, as a minimum an expense is recognised as if the terms had not been modified. In addition, an expense is recognised for any increase in the value of the transaction as a result of the modification, as measured at the date of modification.

Executive LTI Options will vest on a sliding scale so that the amount of options vesting to the individual is dependant on the performance level achieved. Performance is measured over the 24 month period immediately following the grant of the Options, with the following sliding scale applying to the exercise of Executive LTI Options:

- If the minimum annual compound EPS growth rate of 7.5% per annum is not achieved, no Executive LTI Options will vest;
- If the annual compound EPS growth rate is equivalent to 7.5% per annum, 50% of the Executive LTI Options will vest;
- If the annual compound EPS growth rate is equivalent to 12.5% per annum, 100% of the Executive LTI Options will vest; and
- For annual compound EPS growth rate between 7.5% and 12.5% the number of Executive LTI Options which will vest increases pro-rata between 50% and 100%.

The dilutive effect, if any, of outstanding options is reflected as additional share dilution in the computation of earnings per share.

**NOTES TO FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 31 DECEMBER 2011**

**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

**(x) Share-based Payment Transactions (continued)**

**(ii) Performance Options Plan/Deferred Cash Bonus Plans**

The Melbourne IT Ltd Performance Rights Plan and LTI Deferred Cash Bonus Plans (Performance Rights are further described in this report as zero price options and both plans referred to hereafter as "the options") have been established where the managing director and key employees of the company are issued with options to acquire ordinary shares of Melbourne IT Ltd at a nil cost exercise price. The options are issued in accordance with Performance Conditions established by the directors of Melbourne IT Ltd.

The Options have been issued in two tranches and each tranche is subject to a different Performance Condition that must be satisfied before the Options in each tranche vest and are converted into shares. Once the Performance Conditions have been tested and if the Options have vested they will automatically be converted into Melbourne IT shares on the Vesting Date (3 years after the issue date) at a ratio of one option to one ordinary share.

*Relative TSR*

- If the TSR is up to the 50.1 percentile of the companies in the Peer Group, then no Options will vest;
- If the TSR is at the 50.1 percentile of the companies in the Peer Group, then 50% of the Options will vest;
- If the TSR is at the 51st percentile of the companies in the Peer Group, then 52% of the Options will vest;
- If the TSR is at the 74th percentile of the companies in the Peer Group, then 98% of the Options will vest; and
- If the TSR is at the 75th percentile of the companies in the Peer Group, then 100% of the Options will vest.

*EPS*

- If the minimum annual compound EPS growth rate of 7.5% per annum is not achieved, no Options will vest;
- If the annual compound EPS growth rate is equivalent to 7.5% per annum, 50% of the Options will vest;
- If the annual compound EPS growth rate is equivalent to 12.5% per annum, 100% of the Options will vest; and
- For annual compound EPS growth rate between 7.5% and 12.5% the number of Options which will vest increases pro-rata between 50% and 100%.

The fair value is determined by an external valuer using a Monte Carlo Simulation Model. In valuing equity-settled transactions, no account is taken of any performance conditions, other than conditions linked to the price of the shares of Melbourne IT Ltd ('market conditions').

The cost of equity-settled transactions is recognised, together with a corresponding increase in equity, over the period in which the performance conditions are fulfilled, ending on the date on which the relevant employees become fully entitled to the award ('vesting date').

The cumulative expense recognised for equity-settled transactions at each reporting date until vesting date reflects (i) the extent to which the vesting period has expired and (ii) the number of awards that, in the opinion of the directors of Melbourne IT Ltd, will ultimately vest. This opinion is formed based on the best available information at balance date.

No expense is recognised for awards that do not ultimately vest, except for awards where vesting is conditional upon a market condition.

Where the terms of an equity-settled award are modified, as a minimum an expense is recognised as if the terms had not been modified. In addition, an expense is recognised for any increase in the value of the transaction as a result of the modification, as measured at the date of modification.

The dilutive effect, if any, of outstanding Performance Options is reflected as additional share dilution in the computation of earnings per share.

**(iii) Long Term Incentive Deferred Cash Bonus Plan**

The Group also provides benefits to certain employees in the form of cash-settled share based payments, whereby employees render services in exchange for cash, the amounts of which are determined by reference to movements in the price of the shares of Melbourne IT Ltd. The ultimate cost of these cash-settled transactions will be equal to the actual cash paid to the employees, which will be the fair value at settlement date.

The cumulative cost recognised until settlement is a liability and the periodic determination of this liability is as follows:

- (a) At each reporting date between grant and settlement, the fair value of the award is determined
- (b) During the vesting period, the liability recognised at each reporting date is the fair value of the award at that date multiplied by the expired portion of the vesting period
- (c) From the end of the vesting period until settlement, the liability recognised is the full fair value of the liability at the reporting date
- (d) All changes in the liability are recognised in employee benefits expense for the period. The fair value of the liability is determined, initially and at each reporting date until it is settled, by applying an option pricing model, taking into account the terms and conditions on which the award was granted, and the extent to which employees have rendered service to date.

**NOTES TO FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 31 DECEMBER 2011**

**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

**(y) Income Tax**

Current tax assets and liabilities for the current period are measured at the amount expected to be recovered from or paid to the taxation authorities based on the current period's taxable income. The tax rates and tax laws used to compute the amount are those that are enacted or substantively enacted at the reporting date.

Current income tax relating to items recognised directly in equity is recognised in equity and not in profit or loss. Management periodically evaluates positions taken in the tax returns with respect to situations in which applicable tax regulations are subject to interpretation and establishes provisions where appropriate.

Deferred income tax is provided on all temporary differences at the reporting date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes.

Deferred income tax liabilities are recognised for all taxable temporary differences:

- except where the deferred income tax liability arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and
- in respect of taxable temporary differences associated with investments in subsidiaries, associates and interests in joint ventures, except where the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

Deferred income tax assets are recognised for all deductible temporary differences, carry-forward of unused tax assets and unused tax losses, to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, and the carry-forward of unused tax assets and unused tax losses can be utilised:

- except where the deferred income tax asset relating to the deductible temporary difference arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and
- in respect of deductible temporary differences associated with investments in subsidiaries, associates and interests in joint ventures, deferred tax assets are only recognised to the extent that it is probable that the temporary differences will reverse in the foreseeable future and taxable profit will be available against which the temporary differences can be utilised.

The carrying amount of deferred income tax assets is reviewed at each reporting date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred income tax asset to be utilised. Unrecognised deferred income tax assets are reassessed at each reporting date and are recognised to the extent that it has become probable that future taxable profit will allow the deferred tax asset to be recovered.

Deferred income tax assets and liabilities are measured at the tax rates that are expected to apply to the year when the asset is realised or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted at the reporting date. Income taxes relating to items recognised directly in equity are recognised in equity and not in the statement of comprehensive income.

*Tax consolidation legislation*

Melbourne IT Ltd and its wholly-owned Australian controlled entities have implemented the tax consolidation legislation as of 1 January 2006. Members of the tax consolidated group have entered into a tax funding agreement. Each entity is responsible for remitting its share of the current tax payable (receivable) assumed by the head entity.

In accordance with UIG 1052 and Group accounting policy, the Group has applied the "separate taxpayer within group approach" in which the head entity, Melbourne IT Ltd, and the controlled entities in the tax consolidated group continue to account for their own current and deferred tax amounts.

In addition to its own current and deferred tax amounts, Melbourne IT Ltd also recognises the current tax liabilities (or assets) and the deferred tax assets arising from unused tax losses and unused tax credits assumed from controlled entities in the tax consolidated group.

The allocation of taxes to the head entity is recognised as an increase/decrease in the controlled entity's inter-company accounts with the tax consolidated Group head entity.

**(z) Other Taxes**

Revenues, expenses and assets are recognised net of the amount of GST except:

- where the GST incurred on a purchase of goods and services is not recoverable from the taxation authority, in which case the GST is recognised as part of the cost of acquisition of the asset or as part of the expense item as applicable; and
- receivables and payables are stated with the amount of GST included.

The net amount of GST recoverable from, or payable to, the taxation authority is included as part of receivables or payables in the statement of financial position.

Cash flows are included in the Cash Flow Statement on a gross basis and the GST component of cash flows arising from investing and financing activities, which is recoverable from, or payable to, the taxation authority are classified as operating cash flows.

Commitments and contingencies are disclosed net of the amount of GST recoverable from, or payable to, the taxation authority.

**NOTES TO FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 31 DECEMBER 2011**

**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

**(aa) Contributed Equity**

Ordinary share capital is recognised at the fair value of the consideration received by the company. Any transaction costs arising on the issue of ordinary shares are recognised directly in equity as a reduction of the share proceeds received.

**(ab) Option Reserve**

The options reserve is used to recognise the value of equity-settled share based payment transactions provided to employees, including key management personnel, as part of their remuneration. Refer to Note 33 for further details of these plans.

**(ac) Hedging Reserve**

The hedging reserve contains the effective portion of the cash flow hedge relationships incurred as at the reporting date.

**(ad) Foreign Currency Translation Reserve**

The foreign currency translation reserve is used to record exchange differences arising from the translation of the financial statements of foreign subsidiaries.

**(ae) Earnings Per Share**

Basic earnings per share is calculated as net profit attributable to members, adjusted to exclude costs of servicing equity, divided by the weighted average number of ordinary shares, adjusted for any bonus element.

Diluted earnings per share are calculated as net profit attributable to members, adjusted for:

- Cost of servicing equity;
- the after tax effect of dividends and interest associated with dilutive potential ordinary shares that have been recognised as expenses; and
- other non-discretionary changes in revenues or expenses during the period that would result from the dilution of potential ordinary shares;

divided by the weighted average number of ordinary shares and the dilutive potential ordinary shares, adjusted for any bonus element.

**(af) Investment in Associates**

The Group's investment in associates is accounted for using the equity method of accounting in the Group's consolidated financial statements. An associate is an entity over which the Group has a significant influence. It should be noted that on 18 May 2010 the Group purchased the remaining 50% share of the Associate Advantate Pty Ltd.

Under the equity method, the investment in the associate is carried in the consolidated statement of financial position at cost plus post-acquisition changes in the Group's share of the net assets of the associate entity. Goodwill (if applicable) is included in the carrying amount of the investment and is not amortised. After application of the equity method, the Group determines whether it is necessary to recognise any impairment loss with respect to the Groups' net investment in the associate entity.

The Group's share of its associate entity's profit or loss is recognised directly in the profit and loss and its share of movements in reserves is recognised in reserves. The cumulative movements are adjusted against the carrying amount of the investment.

When the Group's share of losses in the associate entity equals or exceeds its interest in the associate, the Group does not recognise further losses, unless it has incurred obligations or made payments on behalf of the associate entity.

**NOTES TO FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 31 DECEMBER 2011**

**2. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES**

The Group's principal financial instruments comprise receivables, payables, promissory notes, interest bearing loans, cash, short-term deposits and derivatives. The Group manages its exposure to key financial risks in accordance with the Group's financial risk management policy. The objective of the policy is to support the delivery of the Group's financial targets whilst protecting financial security.

The purpose is to manage the financial risks arising from the Group's operations. The main risks arising from the Group's financial instruments are interest rate risk, foreign currency risk, liquidity risk and credit risk. The Group uses different methods to measure and manage different types of risks to which it is exposed. These include monitoring levels of exposure to foreign exchange risk and interest rate risk, assessments of market forecasts for foreign exchange and interest rate. Liquidity risk is monitored through the development of rolling cash flow forecasts.

The Board reviews and agrees policies for managing each of these risks as summarised below. Primary responsibility for identification and control of financial risks rests with Management under the supervision of the Audit and Risk Management Committee and under the authority of the Board. The Board reviews and agrees policies for managing each of the risks identified below, including the setting of limits for trading in derivatives, hedging cover of foreign currency and interest rate risk, credit allowances, and cash flow forecast projections.

**Risk Exposures and Responses**

**Interest Rate Risk**

The Group's exposure to market interest rates related primarily to the Group's interest bearing debt, as well as short term deposits held.

At balance date, the Group had the following mix of financial assets and liabilities exposed to variable interest rate risk that are not designated in cash flow hedges.

|  | <b>CONSOLIDATED</b> |               |
|--|---------------------|---------------|
|  | <b>2011</b>         | <b>2010</b>   |
|  | <b>\$'000</b>       | <b>\$'000</b> |
| <b>Financial assets</b>                          |                     |               |
| Cash and cash equivalents                        | 19,047              | 23,379        |
| <b>Financial Liabilities</b>                     |                     |               |
| Interest bearing loans (current and non-current) | 40,291              | 46,246        |
| Less Hedged amounts (Interest Rate Swap) (1)     | (19,654)            | (19,679)      |
| Interest bearing loans - unhedged                | <u>20,637</u>       | <u>26,567</u> |

(1) The Group has a US\$ 20.0 million interest rate swap, exchanging the variable interest rate payable on the US dollar loan for a fixed interest rate. The amount of US\$ 20.0 million has been translated at the year end exchange rate.

**Sensitivity Analysis**

The following sensitivity analysis is based on the interest rate risk exposures in existence at the reporting date.

At 31 December 2011, if interest rates had moved, as illustrated in the table below, with all other variables held constant, post tax profit and equity would have been affected as follows:

|  | <b>Net Profit</b>       |               | <b>Equity</b>           |               |
|--|-------------------------|---------------|-------------------------|---------------|
|  | <b>Higher / (Lower)</b> |               | <b>Higher / (Lower)</b> |               |
|  | <b>2011</b>             | <b>2010</b>   | <b>2011</b>             | <b>2010</b>   |
|  | <b>\$'000</b>           | <b>\$'000</b> | <b>\$'000</b>           | <b>\$'000</b> |
| Consolidated   |                         |               |                         |               |
| Assets + 0.25% (25 basis points), Liabilities + 0.75% (75 basis points), (2010: Assets + 1.5% (150 basis points), Liabilities + 0.7% (70 basis points).                | (71)                    | 152           | (73)                    | 150           |
| Assets - 0.25% (- 25 basis points), Liabilities - 0.25 (-25 basis points), (2010: Assets - 0.5% (- 50 basis points), Liabilities - no reduction in rates anticipated). | (23)                    | (94)          | (22)                    | (94)          |

The sensitivities have been calculated based on average holdings of interest bearing assets and liabilities restated at year end exchange rates. Interest bearing assets are predominantly sensitive to movements in Australian interest rates whilst interest bearing liabilities are predominantly sensitive to movements in US interest rates.

**Credit Risk**

Credit risk arises from the financial assets of the Group, which comprise cash and cash equivalents, trade and other receivables, and derivative instruments. The Group's exposure to credit risk arises from potential default of the counter party, with a maximum exposure equal to the carrying amount of these instruments. Exposure at balance date is addressed in each applicable note.

The Group provides credit only with recognised, creditworthy third parties, and as such collateral is not required nor is it the Group's policy to securitise its trade and other receivables.

It is the Group's policy that all customers who wish to trade on credit terms are subject to credit verification procedures which may include an assessment of their financial position, past experience and industry reputation, depending on the amount of credit to be granted. In addition, receivable balances are monitored on an ongoing basis.

NOTES TO FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 31 DECEMBER 2011

2. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (Continued)

Risk Exposures and Responses (Continued)

Foreign Currency Risk

Due to the prescribed global market arrangements regarding domain name registration, Melbourne IT Limited earns a substantial amount of its revenues, and incurs a substantial amount of its costs in US dollars ("USD") and is therefore exposed to movements in the AUD / USD exchange rate. The company actively manages the gross margin risk by its foreign currency risk management strategy. Please refer to Note 26 for further details.

Both the functional and presentation currency of Melbourne IT Ltd is Australian dollars (A\$). The consolidated Group contains functional currencies as disclosed in note 1(f).

Transactions in foreign currencies are initially recorded in the functional currency at the exchange rates ruling at the date of the transaction.

Monetary assets and liabilities denominated in foreign currencies are retranslated at the rate of exchange ruling at the reporting date.

The exchange differences arising on the retranslation are taken directly to other comprehensive income. On disposal of a foreign entity, the deferred cumulative amount recognised in other comprehensive income relating to that particular foreign operation is recognised in the determination of profit and loss for the year.

At 31 December 2011, the Group had the following exposures to USD denominated assets and liabilities, where the functional currency is not USD. The Group's exposure to foreign currency changes for all other currencies is not material. Assets and liabilities that are that are designated in cashflow hedges are not included:

|                              | CONSOLIDATED   |                |
|------------------------------|----------------|----------------|
|                              | 2011<br>\$'000 | 2010<br>\$'000 |
| <b>Financial Assets</b>      |                |                |
| Cash and cash equivalents    | 4,073          | 585            |
| Trade and Other receivables  | 6,624          | 5,339          |
|                              | <b>10,697</b>  | <b>5,925</b>   |
| <b>Financial Liabilities</b> |                |                |
| Trade and Other Payables     | 9,997          | 6,517          |
| <b>Net exposure</b>          | <b>700</b>     | <b>(592)</b>   |

The following sensitivity is based on foreign currency risk exposures in existence at the reporting date.

At 31 December 2011, had the Australian Dollar moved, as illustrated in the table below, with all other variables held constant, post tax profit and equity would have been affected as follows:

|                             | Net Profit<br>Higher / (Lower) |                | Equity<br>Higher / (Lower) |                |
|-----------------------------|--------------------------------|----------------|----------------------------|----------------|
|                             | 2011<br>\$'000                 | 2010<br>\$'000 | 2011<br>\$'000             | 2010<br>\$'000 |
| Consolidated                |                                |                |                            |                |
| - AUD/USD +8% (2010: + 5%)  | (57)                           | 30             | (57)                       | 30             |
| - AUD/USD -5% (2010: - 10%) | 34                             | (60)           | 34                         | (60)           |

The Group also has exposures to foreign exchange when retranslating foreign currency subsidiaries into Australian Dollars. The sensitivity range has been determined using an expected range of parity to 1.1 USD:AUD for the retranslation of USD denominated balances for the forthcoming year.

NOTES TO FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 31 DECEMBER 2011

2. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (Continued)

Liquidity Risk

Liquidity risk is managed through the establishment of a minimum cash balance and a review of this balance to maximise returns on the available funds. In setting this minimum balance, Management under the supervision of the Audit and Risk Management Committee reviewed the various risks that Melbourne IT faces in achieving its objectives and considered the liquidity required to manage the day-to-day activities of the Group.

The set balance is the specified minimum acceptable surplus of committed facilities/accessible for the next 12 months in each company and globally and will be reviewed annually or earlier upon the occurrence of a significant event. As at 31 December 2011, the Group had external interest bearing debt of US\$41.0 million (2010: US\$47.0 million).

Maturity Analysis of Financial Assets and Liabilities based on Management's Expectation

The risk implied from the values shown in the table below, reflects a balanced view of cash inflows and outflows. Trade payables and other financial liabilities mainly originate from the financing of assets used in ongoing operations such as plant, equipment and investments in working capital e.g. inventories and trade receivables. These assets are considered in the Group's overall liquidity risk. To monitor existing financial assets and liabilities as well as to enable an effective controlling of future risks, the Company has established comprehensive risk reporting covering its worldwide business units that reflects expectations of Management's expected settlement of financial assets and liabilities.

| Consolidated                  | < 6 Months<br>\$'000 | 6 - 12 Months<br>\$'000 | 1 to 5 years<br>\$'000 | > 5 Years<br>\$'000 | Total<br>\$'000 |
|-------------------------------|----------------------|-------------------------|------------------------|---------------------|-----------------|
| <b>31 December 2011</b>       |                      |                         |                        |                     |                 |
| <b>Financial assets</b>       |                      |                         |                        |                     |                 |
| Cash and cash equivalents     | 19,047               | -                       | -                      | -                   | 19,047          |
| Trade and other receivables   | 29,244               | -                       | -                      | -                   | 29,244          |
|                               | <b>48,291</b>        | <b>-</b>                | <b>-</b>               | <b>-</b>            | <b>48,291</b>   |
| <b>Financial liabilities</b>  |                      |                         |                        |                     |                 |
| Trade and other payables      | (21,042)             | -                       | -                      | -                   | (21,042)        |
| Interest and loan liabilities | (3,512)              | (3,476)                 | (34,645)               | -                   | (41,633)        |
|                               | <b>(24,554)</b>      | <b>(3,476)</b>          | <b>(34,645)</b>        | <b>-</b>            | <b>(62,675)</b> |
| <b>Net inflow/(outflow)</b>   | <b>23,737</b>        | <b>(3,476)</b>          | <b>(34,645)</b>        | <b>-</b>            | <b>(14,384)</b> |
| <b>31 December 2010</b>       |                      |                         |                        |                     |                 |
| <b>Financial assets</b>       |                      |                         |                        |                     |                 |
| Cash and cash equivalents     | 23,379               | -                       | -                      | -                   | 23,379          |
| Trade and other receivables   | 24,890               | -                       | -                      | -                   | 24,890          |
|                               | <b>48,269</b>        | <b>-</b>                | <b>-</b>               | <b>-</b>            | <b>48,269</b>   |
| <b>Financial liabilities</b>  |                      |                         |                        |                     |                 |
| Trade and other payables      | (14,532)             | -                       | -                      | -                   | (14,532)        |
| Interest and loan liabilities | (3,544)              | (3,512)                 | (41,602)               | -                   | (48,658)        |
|                               | <b>(18,076)</b>      | <b>(3,512)</b>          | <b>(41,602)</b>        | <b>-</b>            | <b>(63,190)</b> |
| <b>Net inflow/(outflow)</b>   | <b>30,193</b>        | <b>(3,512)</b>          | <b>(41,602)</b>        | <b>-</b>            | <b>(14,921)</b> |

Capital Management

When managing capital, Management's objective is to ensure the entity continues as a going concern as well as to maintain optimal returns to shareholders and benefits for other stakeholders.

Management may change the amount of dividends to be paid to shareholders, issue new shares or sell assets to reduce debt.

During 2011, Management paid dividends of \$10.144 million after the dividend reinvestment plan (2010: \$10.268 million).

Management has no current plans to issue further shares on the market, except for shares issued under the executive and employee share option schemes and dividend reinvestment plan.

Fair Value Hierarchy

Financial instruments at fair value comprise derivative financial instruments whose fair value is derived using valuation techniques whose inputs are based on observable market data.

The preparation of the financial statements requires management to make judgements, estimates and assumptions that affect reported amounts in the financial statements. Management continually evaluates its judgements and estimates in relation to assets, liabilities, contingent liabilities, revenues and expenses. Management bases its judgements and estimates on historical experience and on other various factors it believes to be reasonable under the circumstances, the result of which form the basis of the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions and conditions.

Management has identified the following critical accounting policies for which significant judgements, estimates and assumptions are made. Actual results may differ from these estimates under different assumptions and conditions and may materially affect financial results or the financial position reported in future periods.

Further details of the nature of these assumptions and conditions may be found in the relevant notes to the financial statements.

NOTES TO FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 31 DECEMBER 2011

3. SIGNIFICANT ACCOUNTING JUDGEMENTS, ESTIMATES AND ASSUMPTIONS

(i) Significant accounting judgements

*Taxation*

The Group's accounting policy for taxation requires Management's judgement as to the type of arrangements considered to be a tax on income in contrast to an operating cost. Judgement is also required in assessing whether deferred tax assets and certain deferred tax liabilities are recognised in the statement of financial position. Deferred tax assets are recognised only when it is considered more likely than not that they will be recovered, which is dependant on the generation of sufficient future taxable profits.

Assumptions about the generation of future taxable profits and repatriation of retained earnings depends on Management's estimates of future cash flows. These depend on estimates of future sales volumes, operating costs, capital expenditure, dividends and other capital management transactions. Judgements are also required about the application of income tax legislation. These judgements and assumptions are subject to risk and uncertainty, hence there is a possibility that changes in circumstances will alter expectations, which may impact the amount of deferred tax assets and liabilities recognised in the statement of financial position. In such circumstances, some or all of the carrying amounts of recognised deferred tax assets and liabilities may require adjustment, resulting in a corresponding credit or charge to profit and loss.

(ii) Significant accounting estimates and assumptions

*Impairment of goodwill and intangibles with indefinite useful lives*

The Group determines whether goodwill and intangibles with indefinite useful lives are impaired at least on an annual basis. This requires an estimation of the recoverable amount of the cash-generating unit, using a value in use discounted cashflow methodology, to which the goodwill and intangibles, with indefinite useful lives are allocated. Refer to note 12 for further details of assumptions.

*Share-based payment transactions*

The fair value is determined by an external valuer using a binomial model. In valuing equity-settled transactions, no account is taken of any performance conditions, other than conditions linked to the price of the shares of Melbourne IT Ltd ('market conditions').

The cost of equity-settled transactions is recognised, together with a corresponding increase in equity over the period in which the performance conditions are fulfilled, ending on the date on which the relevant employees become fully entitled to the award ('vesting date').

4. REVENUE

(a) Revenue

|   | CONSOLIDATED   |                |
|---|----------------|----------------|
|   | 2011<br>\$'000 | 2010<br>\$'000 |
| Registration Revenue                    | 65,748         | 74,274         |
| Consulting Revenue                      | 42,414         | 37,620         |
| Hosting & Value-Added Product Sales     | 63,065         | 68,677         |
| For The Record Revenue                  | 7,777          | 7,915          |
| Other Revenue                           | 342            | 676            |
| Total Revenue excluding Interest Income | 179,346        | 189,162        |
| Interest revenue                        | 422            | 631            |
| Total Revenue                           | 179,768        | 189,793        |
| (b) Other income                        |                |                |
| Other                                   | 10             | 69             |
|   | 10             | 69             |
| Total consolidated income               | 179,778        | 189,862        |

NOTES TO FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 31 DECEMBER 2011

5. EXPENSES AND LOSSES / (GAINS)

(a) Depreciation expenses

|  | CONSOLIDATED   |                |
|--|----------------|----------------|
|  | 2011<br>\$'000 | 2010<br>\$'000 |
| Depreciation of non-current assets       |                |                |
| Fit out                                  | 213            | 432            |
| Plant and equipment                      | 4,589          | 5,323          |
| Furniture                                | 52             | 414            |
| Total depreciation of non-current assets | 4,854          | 6,169          |

(b) Amortisation of identifiable intangible assets

|  |       |       |
|--|-------|-------|
| Amortisation of customer contracts                   | 982   | 933   |
| Amortisation of capitalised software                 | 184   | 162   |
| Amortisation of Other Intangibles                    | 105   | 105   |
| Total amortisation of identifiable intangible assets | 1,271 | 1,200 |

Total depreciation and amortisation expenses

|  |        |        |
|--|--------|--------|
| (c) Other Expenses                           |        |        |
| Training & Recruitment                       | 1,027  | 434    |
| Premises                                     | 4,145  | 4,233  |
| Travel & accommodation                       | 2,368  | 1,712  |
| Finance & legal                              | 1,847  | 2,519  |
| Communications                               | 2,298  | 2,217  |
| Equipment                                    | 3,862  | 2,113  |
| Marketing                                    | 2,075  | 2,117  |
| Net foreign currency exchange loss           | 1,203  | 353    |
| Bad and doubtful debts expense / (recovered) | 565    | 698    |
| Interest expense                             | 1,424  | 1,753  |
| Other  | 381    | 869    |
| Total other expenses                         | 21,195 | 19,018 |

(d) Finance costs

|  |     |       |
|--|-----|-------|
| Bank charges and credit card merchant fees | 958 | 1,254 |
|--|-----|-------|

(e) Expensing of share based payments

|  |     |     |
|--|-----|-----|
| Equity & cash settled share based payments | 381 | 785 |
|--|-----|-----|

6. INCOME TAX

The major components of income tax expense are:

(a) Statement of comprehensive income

|  |       |         |
|--|-------|---------|
| Current income tax   |       |         |
| Current income tax charge  | 2,819 | 6,242   |
| Adjustments in respect of current income tax of previous years       | 99    | (1,046) |
| Deferred income tax  |       |         |
| Relating to origination and reversal of temporary differences        | 1,467 | (1,196) |
| Income tax expense reported in the statement of comprehensive income | 4,385 | 4,000   |

(b) Statement of changes in equity

|   |       |    |
|---|-------|----|
| Deferred income tax related to items charged or credited directly to equity |       |    |
| Net gain/(loss) on revaluation of cash flow hedges                          | (102) | 18 |
| Income tax expense reported in equity                                       | (102) | 18 |



NOTES TO FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 31 DECEMBER 2011

|  | CONSOLIDATED   |                |
|--|----------------|----------------|
|  | 2011<br>\$'000 | 2010<br>\$'000 |
| <b>6. INCOME TAX (Continued)</b>   |                |                |
| <b>(c) A reconciliation between tax expense and the product of accounting profit before income tax multiplied by the Group's applicable income tax rate is as follows:</b> |                |                |
| Accounting profit before income tax  | 17,909         | 20,060         |
| At the group's statutory income tax rate of 30% (2010: 30%)  | 5,373          | 6,018          |
| Adjustments in respect of current income tax of previous years   | 99             | (1,046)        |
| Share of net loss of Associate   | -              | 6              |
| Options cost   | 114            | 236            |
| Amortisation of intangibles  | (119)          | (256)          |
| Other Foreign Deductions   | (412)          | (437)          |
| Entertainment  | 26             | 26             |
| Tax Losses not previously brought to account   | (384)          | (214)          |
| Other  | (312)          | (333)          |
|  | <b>4,385</b>   | <b>4,000</b>   |

Income tax expense reported in the statement of comprehensive income

**Tax Consolidation**

Melbourne IT Ltd and its 100% resident subsidiaries formed a tax consolidated Group with effect from 1 January 2006. Melbourne IT Ltd is the head entity of the tax consolidated Group. Members of the Group have entered into a tax sharing agreement that provides for the allocation of income tax liabilities between the entities should the head entity default on its tax payment obligations. No amounts have been recognised in the financial statements in respect of this agreement, on the grounds that the possibility is remote.

The allocation of taxes to the head entity is recognised as an increase/decrease in the controlled entities inter-company accounts with the tax consolidated Group head entity.

Members of the Group have also entered into a tax funding agreement (refer to note 1 (y)).

**Unrecognised temporary differences**

At 31 December 2011, there was \$0.487 million related to unrecognised temporary differences associated with the Group's investments in subsidiaries.

**7. DIVIDENDS PAID OR PROVIDED FOR ON ORDINARY SHARES**

|   |       |       |
|---|-------|-------|
| (a) Dividends paid during the year  |       |       |
| (i) Current year - interim  |       |       |
| Franked dividends (7.0 cents per share) (2010: 7.0 cents)                         | 5,646 | 5,570 |
| (ii) Previous year - final  |       |       |
| Franked dividends (8.0 cents per share) (2010: 8.0 cents per share)               | 6,404 | 6,320 |
| (b) Dividends proposed and not recognised as a liability                          |       |       |
| Franked dividends (8.0 cents per share) (2010: 8.0 cents)                         | 6,508 | 6,403 |
| (c) Franking credit balance   |       |       |
| The amount of franking credits available for the subsequent financial year are:   |       |       |
| - franking account balance as at the end of the financial year at 30% (2010: 30%) | 6,428 | 8,659 |

At the 21 February 2012 Board Meeting, the directors declared a 8.0 cents fully franked final dividend on ordinary shares in respect of the year ended 31 December 2011.

In accordance with the accounting standards, the total amount of this final dividend of \$6.508 million has not been provided for in the 31 December 2011 financial statements. There will be a \$2.789 reduction in the franking credits available for future reporting period on the 8.0 cents per share dividend proposed before the financial report was authorised but not recognised as a distribution to equity holders during the period.

NOTES TO FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 31 DECEMBER 2011

|   | CONSOLIDATED   |                |
|---|----------------|----------------|
|   | 2011<br>\$'000 | 2010<br>\$'000 |
| <b>8. TRADE AND OTHER RECEIVABLES (CURRENT)</b>                             |                |                |
| Trade debtors   | 30,591         | 26,361         |
| Allowance for impairment loss   | (1,347)        | (1,471)        |
|   | <b>29,244</b>  | <b>24,890</b>  |
| <i>Terms and conditions</i>   |                |                |
| Terms and conditions relating to the above financial instruments            |                |                |
| i. Trade debtors are non-interest bearing and generally on 14-60 day terms. |                |                |
| ii. Allowance for impairment loss   |                |                |
| Movements in the provision for impairment loss were as follows:             |                |                |
| Opening Balance   | 1,471          | 1,830          |
| Additional Provision / (Released)   | 215            | (31)           |
| Amounts Written off   | (333)          | (211)          |
| Foreign currency translation impact   | (6)            | (117)          |
| Closing Balance   | <b>1,347</b>   | <b>1,471</b>   |

At 31 December, the ageing analysis of trade receivables is as follows:

| Consolidated           | 2011            |                     | 2010            |                     |
|------------------------|-----------------|---------------------|-----------------|---------------------|
|                        | Gross<br>\$'000 | Allowance<br>\$'000 | Gross<br>\$'000 | Allowance<br>\$'000 |
| <b>Current</b>         | 18,527          | -                   | 13,730          | (10)                |
| 0 - 30 days past due   | 6,637           | -                   | 5,920           | (10)                |
| 31 - 60 days past due  | 2,164           | -                   | 2,117           | (11)                |
| Past due 61 days +     | 3,263           | (1,347)             | 4,594           | (1,440)             |
| <b>Closing Balance</b> | <b>30,591</b>   | <b>(1,347)</b>      | <b>26,361</b>   | <b>(1,471)</b>      |

Receivables past due but not considered impaired are \$10.717 million, and comprise balances owed from customers who have a good history of repayments or are otherwise considered recoverable.

Due to the short-term nature of these receivables, their carrying value is assumed to approximate their fair value. The maximum exposure to credit risk is the fair value of receivables. Collateral is not held as security.

|                                   | CONSOLIDATED   |                |
|-----------------------------------|----------------|----------------|
|                                   | 2011<br>\$'000 | 2010<br>\$'000 |
| <b>9. INVENTORIES</b>             |                |                |
| Materials (at cost)               | <b>463</b>     | <b>562</b>     |
| <b>10. OTHER ASSETS (CURRENT)</b> |                |                |
| Other prepayments                 | 3,674          | 2,514          |
| GST receivable                    | 173            | 299            |
|                                   | <b>3,847</b>   | <b>2,813</b>   |

NOTES TO FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 31 DECEMBER 2011

|  | CONSOLIDATED   |                |
|--|----------------|----------------|
|  | 2011<br>\$'000 | 2010<br>\$'000 |
| <b>11. PROPERTY, PLANT AND EQUIPMENT (NON-CURRENT)</b>   |                |                |
| Leasehold improvements   |                |                |
| At cost  | 3,394          | 4,844          |
| Accumulated amortisation   | (3,107)        | (4,535)        |
|  | <b>287</b>     | <b>309</b>     |
| Plant and equipment  |                |                |
| At cost  | 31,794         | 38,951         |
| Accumulated depreciation   | (26,837)       | (31,720)       |
|  | <b>4,957</b>   | <b>7,231</b>   |
| Furniture and fittings   |                |                |
| At cost  | 794            | 1,020          |
| Accumulated depreciation   | (678)          | (895)          |
|  | <b>116</b>     | <b>125</b>     |
| Total property, plant and equipment  |                |                |
| At cost  | 35,982         | 44,815         |
| Accumulated depreciation and amortisation  | (30,622)       | (37,150)       |
| Total written down amount  | <b>5,360</b>   | <b>7,665</b>   |
| <b>Reconciliations</b>   |                |                |
| Reconciliations of the carrying amounts of leasehold improvements, plant and equipment and furniture/fittings at the beginning and end of the current and previous financial year. |                |                |
| Leasehold improvements   |                |                |
| Carrying amount at beginning   | 309            | 676            |
| Additions  | 195            | 241            |
| Transfer / other   | 12             | (140)          |
| Disposals  | (11)           | (33)           |
| Foreign exchange differences   | (5)            | (3)            |
| Depreciation expense   | (213)          | (432)          |
|  | <b>287</b>     | <b>309</b>     |
| Plant and Equipment  |                |                |
| Carrying amount at beginning   | 7,231          | 10,396         |
| Additions  | 2,484          | 3,876          |
| Transfer / other   | (12)           | (49)           |
| Disposals  | (169)          | (1,530)        |
| Foreign exchange differences   | 12             | (139)          |
| Depreciation expense   | (4,589)        | (5,323)        |
|  | <b>4,957</b>   | <b>7,231</b>   |
| Furniture and Fittings   |                |                |
| Carrying amount at beginning   | 125            | 102            |
| Additions  | 58             | 64             |
| Transfer / other   | -              | 395            |
| Disposals  | (6)            | (14)           |
| Foreign exchange differences   | (9)            | (8)            |
| Depreciation expense   | (52)           | (414)          |
|  | <b>116</b>     | <b>125</b>     |
| Total written down amount  | <b>5,360</b>   | <b>7,665</b>   |

NOTES TO FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 31 DECEMBER 2011

|  | CONSOLIDATED      |                      |                    |                            |                |                |
|--|-------------------|----------------------|--------------------|----------------------------|----------------|----------------|
|  | 2011<br>\$'000    | 2010<br>\$'000       |                    |                            |                |                |
| <b>12. INTANGIBLE ASSETS</b>   |                   |                      |                    |                            |                |                |
| <b>(a) Carrying amounts of intangible assets</b>   |                   |                      |                    |                            |                |                |
| Total Intangible Assets  |                   |                      |                    |                            | <b>130,661</b> | <b>126,641</b> |
| <b>Reconciliation of carrying amounts at the beginning and end of the period</b>   |                   |                      |                    |                            |                |                |
|  | Other Intangibles | Capitalised Software | Customer Contracts | Market Related Intangibles | Goodwill       | Total          |
|  | \$'000            | \$'000               | \$'000             | \$'000                     | \$'000         | \$'000         |
| <b>Year ended 31 December 2011</b>   |                   |                      |                    |                            |                |                |
| Net balance at 1 January 2011  | 158               | 6,122                | 7,509              | 9,982                      | 102,870        | 126,641        |
| Acquisitions and Additions   | -                 | 5,710                | -                  | -                          | -              | 5,710          |
| Amortisation   | (105)             | (184)                | (982)              | -                          | -              | (1,271)        |
| Foreign exchange impact  | -                 | (5)                  | 50                 | -                          | (464)          | (419)          |
| <b>Net balance at 31 December 2011</b>   | <b>53</b>         | <b>11,643</b>        | <b>6,577</b>       | <b>9,982</b>               | <b>102,406</b> | <b>130,661</b> |
| <b>Year ended 31 December 2010</b>   |                   |                      |                    |                            |                |                |
| Net balance at 1 January 2010  | 263               | 728                  | 9,479              | 9,982                      | 109,070        | 129,522        |
| Acquisitions and Additions   | -                 | 5,683                | -                  | -                          | 673            | 6,356          |
| Amortisation   | (105)             | (427)                | (668)              | -                          | -              | (1,200)        |
| Foreign exchange impact  | -                 | 138                  | (1,302)            | -                          | (6,873)        | (8,037)        |
| <b>Net balance at 31 December 2010</b>   | <b>158</b>        | <b>6,122</b>         | <b>7,509</b>       | <b>9,982</b>               | <b>102,870</b> | <b>126,641</b> |
| <b>(b) Capitalised Software: Assets Under Construction - Transformation Projects</b>   |                   |                      |                    |                            |                |                |
| Melbourne IT Ltd is currently undertaking a significant investment in infrastructure, innovation, and transformational projects which will provide the platform for the Group's next phase of growth.  |                   |                      |                    |                            |                |                |
| The most significant transformation project is Integrated Web Services (IWS), which will enable Melbourne IT to fully leverage the value of the Group's customer base by allowing the business to sell customers the full suite of services across business units and geographies. It is a significant investment over three years that will transform the systems that are used to sell to and support the Group's customers, in addition to the implementation of a common financial reporting system (Oracle Financials) across all entities. |                   |                      |                    |                            |                |                |
| Operational Support Systems (OSS) project will improve infrastructure stability and allow the organisation to manage a greater variety of products and services.   |                   |                      |                    |                            |                |                |
| In line with AASB 138 Intangible Assets, costs relating to the research phase of the project are expensed while costs relating to the development phase are capitalised as Capitalised Software: Assets Under Construction - Transformation Projects. Once the project is operational, hardware will be amortised over a 4 year period and software/intellectual property will be amortised over a 5 year period. There was no amortisation in the year ended 31 December 11 in relation to these intangible assets.                             |                   |                      |                    |                            |                |                |

**NOTES TO FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 31 DECEMBER 2011**

**12. INTANGIBLE ASSETS (Continued)**

**(c) Goodwill and intangible assets impairment testing**

**Goodwill -Domainz Ltd**

Goodwill of the amount of \$0.720 million has been allocated to this cash generating unit ('CGU') for the purposes of impairment testing. The recoverable amount of Domainz Ltd has been determined based on a value in use calculation using cash flow projections based on financial budgets approved by the Board covering a five year period.

The discount rate applied to cash flow projections is 13.2% (2010: 13%) and cash flows beyond the five year period are extrapolated using a 3% growth rate (2010: 3%) to determine terminal value, which is the company's estimate of the long term average growth rate for the industry in which the company operates. At the current time, Management believe that no reasonably possible change in any of the above assumptions would cause the recoverable value of goodwill relating to Domainz Ltd to fall materially below its carrying amount.

**Goodwill - Melbourne IT DBS Group (including Melbourne IT DBS Group AB, IDR Management Services Ltd & DBMS Group - "Melbourne IT DBS Group")**

Goodwill of the amount of \$44.527 million has been allocated to this CGU for impairment testing purposes. The recoverable amount of Melbourne IT DBS Group has been determined based on a value in use calculation using cash flow projections based on financial budgets approved by the Board covering a five year period.

The discount rate applied to cash flow projections is 13.2% (2010: 13%) and cash flows beyond the five year period are extrapolated using a 3% growth rate (2010: 3%) to determine terminal value, which is the company's estimate of the long term average growth rate for the industry in which the company operates. At the current time, Management believe that no reasonably possible change in any of the above assumptions would cause the recoverable value of goodwill relating to Melbourne IT DBS Group to fall materially below its carrying amount.

**Goodwill and Market Related Intangibles - WebCentral Group Pty Ltd**

Goodwill and market related intangibles of the amount of \$67.472 million have been allocated to the CGUs for the purposes of impairment testing. WebCentral Group Pty Ltd contains two legal entities, being WebCentral and For the Record,

**- WebCentral**

The WebCentral (\$50.884 million goodwill and \$7.128 million market related intangibles) legal entity's performance is measured at both a legal entity level and also measured as participating in the following business units: SMB, GPS and ES, which include the cash flows from both WebCentral and Melbourne IT legal entities. These disclosed business unit segments represents the lowest level at which Management views the WebCentral business, and therefore the lowest level at which goodwill attributable to WebCentral is monitored and tested for impairment. The recoverable amount of the WebCentral Group Pty Ltd CGUs is based on a value in use calculation using cash flow projections and financial budgets approved by the Board covering a five year period.

The discount rate applied to cash flow projections is 13.2% (2010: 13%) and cash flows beyond the five year period are extrapolated using a 3% growth rate (2010: 3%) to determine terminal value, which is the company's estimate of the long term average growth rate for the industry in which the company operates. At the current time, Management believe that no reasonably possible change in any of the above assumptions would cause the recoverable value of goodwill relating to WebCentral Group Pty Ltd to fall materially below its carrying amount.

**- For the Record**

For the Record (\$5.601 million goodwill and \$2.880 million market related intangibles) is a stand-alone business unit and represents a single CGU which is tested for impairment. The recoverable amount of For the Record has been determined based on a value in use calculation using cash flow projections based on financial budgets approved by the Board covering a five year period.

The discount rate applied to cash flow projections is 14.2% (2010: 13%) and cash flows beyond the five year period are extrapolated using a 3% growth rate (2010: 3%) to determine terminal value, which is the company's estimate of the long term average growth rate for the industry in which the company operates. A variation of 10% in management's best estimate of future cash flows may cause the recoverable value of goodwill relating to For the Record to fall materially below its carrying amount.

**Key assumptions used in value in use calculations**

Value in use calculations used cash flow projections based on financial budgets approved by the Board covering a five year period. These budgets are most sensitive to the following assumptions:

- Revenue growth
- Wage growth

The assumptions by Management were based on historical experience in the industry with a view of the current and future economic climate.

**NOTES TO FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 31 DECEMBER 2011**

**13. DEFERRED TAX ASSET (NON-CURRENT)**

Deferred tax asset at 31 December relates to the following:

|                          | 2011<br>\$'000 | 2010<br>\$'000 |
|--------------------------|----------------|----------------|
| Doubtful debts provision | 404            | 441            |
| Employee benefits        | 1,615          | 1,464          |
| Accruals                 | 637            | 730            |
| Tax losses               | 2,454          | 989            |
| Interest payable         | -              | 898            |
| Depreciation             | 484            | 392            |
| Unrealised FX            | 754            | 803            |
| Hedging reserve          | 333            | 543            |
| Other                    | (145)          | (289)          |
|                          | <b>6,536</b>   | <b>5,971</b>   |

**Tax losses**

As at 31 December 2011 the Group has tax losses which arose in Melbourne IT DBS ApS of \$1.085 million (2010: \$1.085 million), Melbourne IT DBS Ltd of \$1.119 million (2010: \$0.936 million) and Melbourne IT DBS SAS of \$1.216 million (2010: \$2.085 million) that are available for offset against future taxable profits of the companies in which the losses arose. However, these losses relate to subsidiaries that have a history of losses and may not be used to offset taxable income elsewhere in the Group.

Deferred tax assets have not been recognised in respect of these losses as they may not be used to offset taxable profits elsewhere in the Group and they have arisen in subsidiaries that have been loss-making in the past. The subsidiary has no taxable temporary differences nor any tax planning opportunities available that could partly support the recognition of these losses as deferred tax assets. If the Group were able to recognise all unrecognised deferred tax assets, profit would increase by \$0.972 million.

**14. OTHER ASSETS (NON-CURRENT)**

|             |           |           |
|-------------|-----------|-----------|
| Rental bond | <b>58</b> | <b>43</b> |
|-------------|-----------|-----------|

**15. TRADE AND OTHER PAYABLES (CURRENT)**

|                              |               |               |
|------------------------------|---------------|---------------|
| Trade creditors              | 3,236         | 2,441         |
| Sundry creditors             | 8,655         | 4,718         |
| Deposits received in advance | 3,079         | 1,733         |
| Accrued expenses             | 6,072         | 5,640         |
| Total payables               | <b>21,042</b> | <b>14,532</b> |

- (a) Terms and conditions relating to trade creditors:  
 (i) Trade creditors are non-interest bearing and are normally settled within agreed trading terms.  
 (ii) Sundry creditors are non-interest bearing and are normally settled within agreed trading terms.

**16. INTEREST-BEARING LOANS AND BORROWINGS**

**Current**

|                         |              |              |
|-------------------------|--------------|--------------|
| US Dollar Currency Loan | 5,896        | 5,904        |
|                         | <b>5,896</b> | <b>5,904</b> |

**Non-current**

|                             |               |               |
|-----------------------------|---------------|---------------|
| US Dollar Currency Loan (i) | 34,395        | 40,342        |
|                             | <b>34,395</b> | <b>40,342</b> |

**(a) Terms and conditions**

- (i) The US Dollars Overseas Currency Loan US\$41.0 million:  
 - In line with the loan agreement, Melbourne IT has made four repayments of USD \$1.5 million, total USD \$6.0 million, during the year.  
 - For the year ended 31 December 2011, the average interest rate was 3.16%.

- The Group has complied with bank covenants during the year ended 31 December 2011.

- This loan is unsecured and payable in full on 30 April 2013.

**(b) Financing facilities available**

At reporting date, the following financing facilities had been negotiated and were available:

|                                      |               |               |
|--------------------------------------|---------------|---------------|
| Total facilities                     |               |               |
| - Asset Finance - leasing            | 6,200         | 5,500         |
| - Business Lending - Bank Guarantees | 1,708         | 1,675         |
| - Standby Letters of Credit          | 4,861         | 8,049         |
|                                      | <b>12,769</b> | <b>15,224</b> |
| Facility used at reporting date      |               |               |
| - Asset Finance - leasing            | 719           | -             |
| - Business Lending - Bank Guarantees | 1,187         | 895           |
| - Standby Letters of Credit          | 3,878         | 4,239         |
|                                      | <b>5,784</b>  | <b>5,134</b>  |

NOTES TO FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 31 DECEMBER 2011

|   | CONSOLIDATED      |                |                   |               |
|---|-------------------|----------------|-------------------|---------------|
|   | 2011<br>\$'000    | 2010<br>\$'000 |                   |               |
| <b>17. PROVISIONS (CURRENT)</b>                                 |                   |                |                   |               |
| Employee benefits   | 4,568             | 4,165          |                   |               |
| <b>18. CURRENT TAX LIABILITIES</b>                              |                   |                |                   |               |
| Income tax  | 568               | 904            |                   |               |
| <b>19. DEFERRED TAX LIABILITY (NON-CURRENT)</b>                 |                   |                |                   |               |
| Deferred tax liability at 31 December relates to the following: |                   |                |                   |               |
| Intangible assets   | 4,111             | 2,194          |                   |               |
| Other   | 115               | -              |                   |               |
|   | <b>4,226</b>      | <b>2,194</b>   |                   |               |
| <b>20. PROVISIONS (NON-CURRENT)</b>                             |                   |                |                   |               |
| Employee benefits   | 815               | 716            |                   |               |
| <b>21. CONTRIBUTED EQUITY</b>                                   |                   |                |                   |               |
| (a) Issued and paid-up capital                                  |                   |                |                   |               |
| Ordinary shares each fully paid                                 | 66,900            | 64,839         |                   |               |
| (b) Movements in shares on issue                                |                   |                |                   |               |
|   | 2011              | 2010           |                   |               |
|   | No. of<br>Shares  | \$'000         | No. of<br>Shares  | \$'000        |
| Beginning of the financial year                                 | 80,031,955        | 64,839         | 78,970,419        | 63,005        |
| Issued during the year:   |                   |                |                   |               |
| - Dividend Reinvestment Plan                                    | 1,227,323         | 1,906          | 887,136           | 1,622         |
| - Executive and employee options exercised                      | 92,900            | 155            | 174,400           | 212           |
| <b>End of the financial year</b>                                | <b>81,352,178</b> | <b>66,900</b>  | <b>80,031,955</b> | <b>64,839</b> |

**Other capital reserves**

*Options reserve*

During the financial year 930,000 (2010: 910,000) options were issued over ordinary shares. At the end of the year there were 4,949,104 (2010: 5,101,654) unissued ordinary shares in respect of which options were outstanding. (Details are provided in Note 33).

*Hedging reserve*

The hedge reserve contains the effective portion of the hedge relationships incurred as at the reporting date. The \$238,000 reduction in the reserve is made up of the net 2011 movements in forward currency contracts and the effective proportion of the interest rate swap contract, net of tax. The 2010 increase in reserve of \$42,000 corresponds also to the net movement in these hedge instruments.

*Foreign currency translation reserve*

The foreign currency translation reserve is used to record exchange differences arising from the translation of the financial statements of foreign subsidiaries.

NOTES TO FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 31 DECEMBER 2011

|  | CONSOLIDATED   |                |
|--|----------------|----------------|
|  | 2011<br>\$'000 | 2010<br>\$'000 |
| <b>22. CASH FLOW STATEMENT</b>   |                |                |
| <b>(a) Reconciliation of the operating profit after tax to the net cash flow from operations:</b>  |                |                |
| Operating profit after tax   | 13,524         | 16,060         |
| Depreciation of non-current assets   | 4,854          | 6,169          |
| Amortisation of non-current assets   | 1,271          | 1,200          |
| Expense of share based payments  | 381            | 785            |
| Loss from associate  | -              | 20             |
| Changes in assets and liabilities  |                |                |
| Increase in trade debtors  | (4,354)        | (776)          |
| Decrease in inventories  | 99             | 20             |
| Decrease in prepayments  | 2,927          | 3,644          |
| Decrease in deferred revenue   | (5,475)        | (2,022)        |
| Increase in provision for employee entitlements  | 502            | 527            |
| Increase in deferred tax asset   | (565)          | (2,949)        |
| Increase in deferred tax liability   | 2,032          | 2,194          |
| Increase (decrease) in accounts payable  | 3,942          | (3,062)        |
| Decrease Income tax provision  | (336)          | (1,149)        |
| Increase (decrease) in income received in advance  | 1,346          | (1,666)        |
| Increase in other assets   | (1,049)        | (267)          |
| <b>Net cash flow from operating activities</b>   | <b>19,099</b>  | <b>18,729</b>  |
| <b>(b) Reconciliation of cash and cash equivalents</b>   |                |                |
| For the purposes of the Cash Flow Statement, cash and cash equivalents comprise the following:   |                |                |
| Cash and cash equivalents on hand  | 19,047         | 23,379         |
| <b>Closing cash and cash equivalents balances</b>  | <b>19,047</b>  | <b>23,379</b>  |
| <b>23. BUSINESS COMBINATIONS</b>   |                |                |
| <b>Change in composition of Melbourne IT Ltd</b>   |                |                |
| <b>2010</b>  |                |                |
| On 18 May 2010, Melbourne IT purchased the remaining 50% share of the associate Advantate Pty Ltd. Effective 19 May 2010, Advantate ceased being an associate and became a 100% subsidiary. Activities from this business are no longer equity accounted as an associate, but consolidated into the SMB business unit. The impact on the Group's financial position and financial performance for 2010 was immaterial. |                |                |

NOTES TO FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 31 DECEMBER 2011

24. EXPENDITURE COMMITMENTS AND OBLIGATIONS

Lease expenditure commitments

Operating leases

|  |               |               |
|--|---------------|---------------|
| Minimum lease payments                                       |               |               |
| - not later than one year                                    | 5,757         | 5,432         |
| - later than one year and not later than five years          | 12,824        | 14,582        |
| - later than five years                                      | 3,466         | 2,711         |
| Aggregate lease expenditure contracted for at reporting date | <u>22,047</u> | <u>22,725</u> |

Financial instruments

The details of hedging instruments held and guarantees issued are as follows:

(a) Hedging instruments

Hedges of specific commitments

Melbourne IT Ltd earns a substantial amount of its revenues, and incurs a substantial amount of its costs in US dollars ("USD") and is therefore exposed to movements in the AUD / USD dollar exchange rate. The company actively manages the gross margin risk by its foreign currency risk management strategy.

As at 31 December 2011, Melbourne IT Ltd has entered into a number of foreign currency exchange contracts with the primary objective of minimising the impact of foreign currency fluctuations on the Group's ability to achieve its objectives in the financial year.

The contracts have been treated in accordance with cashflow hedge accounting, as the approximate value of the purchase and entities with which the transactions will be entered is presently known.

The Group has also entered into a USD \$20.0 million interest rate swap, exchanging the variable rate payable on USD \$20.0 million of the USD \$41.0 million interest bearing liability for a fixed rate. The transaction reduces the Group's exposure to fluctuation in variable interest rates over the longer term.

The derivatives have been determined as being effective hedges and have been accounted for in accordance with AASB 139.

(b) Financial Guarantees and other credit facilities

Financial guarantees and other credit facilities have been assessed at fair value and are disclosed as follows.

- (a) The company has Standby Letters of Credit totalling US\$2.7 million in accordance with various Registry Licence Agreements. These Standby Letters of Credit are due to expire on 30 June 2012, at which time it is expected that they will be renewed for another 12 months.
- (b) Bank Guarantees of AU\$1.187 million have been issued in favour of various parties in accordance with the Group's property commitments.
- (c) A Standby Letter of Credit of US\$1.2 million has been issued in favour of Wells Fargo Bank Inc. in accordance with the provision of Domain Name Registry Credit Card commitments as well as other banking facilities within the United States.

25. EMPLOYEE BENEFITS AND SUPERANNUATION COMMITMENTS

The aggregate employee benefit liability comprises:

|                          |              |              |
|--------------------------|--------------|--------------|
|                          | CONSOLIDATED |              |
|                          | 2011         | 2010         |
|                          | \$'000       | \$'000       |
| Provisions (current)     | 4,568        | 4,165        |
| Provisions (non-current) | 815          | 716          |
|                          | <u>5,383</u> | <u>4,881</u> |

NOTES TO FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 31 DECEMBER 2011

26. DERIVATIVE FINANCIAL INSTRUMENTS

Hedging Activities

2011

(a) Cash flow hedge

At 31 December 2011, Melbourne IT Ltd held seven foreign exchange contracts designated as cash flow hedges of expected future sales to customers in the US for which the company has firm commitments.

The exchange contracts are being used to reduce the exposure of foreign exchange risk. The terms of these contracts are as follows:

| Sell   | Maturity Date    | Protection Rate | Advantage Rate  | Value of Hedge as at 31 Dec 2011 (\$) |
|--|------------------|-----------------|-----------------|---------------------------------------|
| US\$325,000  | 31 January 2012  | A\$/US\$ 0.9990 | A\$/US\$ 0.9730 | 7,972                                 |
| US\$325,000  | 27 February 2012 | A\$/US\$ 1.0590 | A\$/US\$ 1.0335 | (10,266)                              |
| US\$325,000  | 30 March 2012    | A\$/US\$ 1.0300 | A\$/US\$ 0.9920 | (493)                                 |
| US\$150,000  | 30 April 2012    | A\$/US\$ 0.9480 | A\$/US\$ 0.9100 | 10,391                                |
| US\$175,001  | 26 April 2012    | A\$/US\$ 1.0375 | A\$/US\$ 1.0025 | (3,124)                               |
| US\$325,000  | 29 May 2011      | A\$/US\$ 0.9950 | A\$/US\$ 0.9670 | 4,257                                 |
| US\$325,000  | 29 June 2011     | A\$/US\$ 1.0000 | A\$/US\$ 0.9600 | 5,467                                 |
| Total value of unrealised foreign exchange contracts |                  |                 |                 | <u>14,204</u>                         |

The terms of these foreign exchange contracts have been negotiated to match the terms of the commitments.

As at 31 December 2011, an unrealised gain of \$14,204 (2010: gain of \$258,182) is included in other comprehensive income in respect of these contracts.

(b) Interest rate hedges

As at 31 December 2011, the Group held one interest rate swap contract of US\$20.0 million (2010: US\$20.0 million) designed to hedge the variable interest rate exposure relating to the interest bearing liabilities of US\$41.0 million (2010: US\$47.0 million).

| Notional amount                        | Termination Date | Fixed Rate | Floating Rate | Value of Hedge as at 31 Dec 2011 (\$) |
|--|------------------|------------|---------------|---------------------------------------|
| US\$20,000,000                         | 30 April 2013    | 2.14%      | USD LIBOR BBA | (438,755)                             |
| Total Derivative financial instruments |                  |            |               | <u>(424,551)</u>                      |

2010

(a) Cash flow hedge

At 31 December 2010, Melbourne IT Ltd held six foreign exchange contracts designated as cash flow hedges of expected future sales to customers in the United States for which the company has firm commitments.

The exchange contracts were being used to reduce the exposure of foreign exchange risk. The terms of these contracts were as follows:

| Sell   | Maturity Date    | Protection Rate | Advantage Rate  | Value of Hedge as at 31 Dec 2010 (\$) |
|--|------------------|-----------------|-----------------|---------------------------------------|
| US\$600,000  | 31 January 2011  | A\$/US\$ 0.8935 | A\$/US\$ 0.8685 | 83,056                                |
| US\$600,000  | 28 February 2011 | A\$/US\$ 0.8810 | A\$/US\$ 0.8520 | 90,404                                |
| US\$600,000  | 31 March 2011    | A\$/US\$ 0.9695 | A\$/US\$ 0.9295 | 29,614                                |
| US\$600,000  | 27 April 2011    | A\$/US\$ 0.9730 | A\$/US\$ 0.9350 | 25,911                                |
| US\$600,000  | 31 May 2011      | A\$/US\$ 0.9755 | A\$/US\$ 0.9355 | 22,828                                |
| US\$600,000  | 30 June 2011     | A\$/US\$ 0.9930 | A\$/US\$ 0.9630 | 6,369                                 |
| Total value of unrealised foreign exchange contracts |                  |                 |                 | <u>258,182</u>                        |

The terms of the foreign exchange contracts had been negotiated to match the terms of the commitments.

(b) Interest rate hedges

As at 31 December 2010, the Group held one interest rate swap contract of US\$20.0 million (2009: US\$20.0 million) designed to hedge the variable interest rate exposure relating to the interest bearing liabilities of US\$47.0 million (2009: US\$52.0 million).

| Notional amount                        | Termination Date | Fixed Rate | Floating Rate | Value of Hedge as at 31 Dec 2010 (\$) |
|--|------------------|------------|---------------|---------------------------------------|
| US\$20,000,000                         | 30 April 2013    | 2.14%      | USD LIBOR BBA | (597,100)                             |
| Total Derivative financial instruments |                  |            |               | <u>(338,918)</u>                      |

**NOTES TO FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 31 DECEMBER 2011**
**27. OPERATING SEGMENT**
**Operating Segment - Continuing Operations**

The following table presents the revenue and profit information regarding business unit segments for the years ended 31 December 2011 and 31 December 2010.

| Year ended 31 December 2011              | SMB        | GPS        | DBS        | ES        | FTR        | Total          |
|--|------------|------------|------------|-----------|------------|----------------|
|  | \$'000     | \$'000     | \$'000     | \$'000    | \$'000     | \$'000         |
| <b>Segment revenue</b>                   |            |            |            |           |            |                |
| Revenue from operating activities        |            |            |            |           |            |                |
| Registration Revenue                     | 20,494     | 33,457     | 11,797     | -         | -          | 65,748         |
| Consulting Revenue                       | -          | -          | 42,414     | -         | -          | 42,414         |
| Hosting & Value-Added Product Sales      | 19,967     | 15,166     | 1,115      | 26,817    | -          | 63,065         |
| For The Record Revenue                   | -          | -          | -          | -         | 7,777      | 7,777          |
| Other Revenue                            | 330        | 4          | 8          | -         | -          | 342            |
| Total segment revenue                    | 40,791     | 48,627     | 55,334     | 26,817    | 7,777      | 179,346        |
| Interest revenue                         |            |            |            |           |            | 422            |
| Other income                             |            |            |            |           |            | 10             |
| <b>Total consolidated revenue</b>        |            |            |            |           |            | <b>179,778</b> |
| <b>Result</b>                            |            |            |            |           |            |                |
| Segment results                          | 8,258      | 7,128      | 8,978      | 1,710     | 1,198      | 27,272         |
| Unallocated expenses                     |            |            |            |           |            | (5,363)        |
| - Corporate                              |            |            |            |           |            | (2,998)        |
| - Transformation Projects                |            |            |            |           |            |                |
| Earnings before interest and tax         |            |            |            |           |            | 18,911         |
| <b>Net Interest</b>                      |            |            |            |           |            |                |
| Interest revenue                         |            |            |            |           |            | 422            |
| Interest expense                         |            |            |            |           |            | (1,424)        |
| Total Net Interest                       |            |            |            |           |            | (1,002)        |
| Income tax expense                       |            |            |            |           |            | (4,385)        |
| <b>Net Profit for the year</b>           |            |            |            |           |            | <b>13,524</b>  |
| <b>Year ended 31 December 2010</b>       | <b>SMB</b> | <b>GPS</b> | <b>DBS</b> | <b>ES</b> | <b>FTR</b> | <b>Total</b>   |
|  | \$'000     | \$'000     | \$'000     | \$'000    | \$'000     | \$'000         |
| <b>Segment revenue</b>                   |            |            |            |           |            |                |
| Revenue from operating activities        |            |            |            |           |            |                |
| Registration Revenue                     | 21,554     | 40,287     | 12,433     | -         | -          | 74,274         |
| Consulting Revenue                       | -          | -          | 37,620     | -         | -          | 37,620         |
| Hosting & Value-Added Product Sales      | 20,808     | 15,357     | 951        | 31,561    | -          | 68,677         |
| For The Record Revenue                   | -          | -          | -          | -         | 7,915      | 7,915          |
| Other Revenue                            | 360        | 198        | 61         | 57        | -          | 676            |
| Total segment revenue                    | 42,722     | 55,842     | 51,065     | 31,618    | 7,915      | 189,162        |
| Interest revenue                         |            |            |            |           |            | 631            |
| Other income                             |            |            |            |           |            | 69             |
| <b>Total consolidated revenue</b>        |            |            |            |           |            | <b>189,862</b> |
| <b>Result</b>                            |            |            |            |           |            |                |
| Segment results                          | 9,448      | 8,253      | 6,370      | 3,536     | -          | 27,577         |
| Share of Advantate Pty Ltd - (50% owned) |            |            |            |           |            | (20)           |
| Unallocated expenses                     |            |            |            |           |            | (4,633)        |
| - Corporate                              |            |            |            |           |            | (1,742)        |
| - Transformation Projects                |            |            |            |           |            |                |
| Earnings before interest and tax         |            |            |            |           |            | 21,182         |
| <b>Net Interest</b>                      |            |            |            |           |            |                |
| Interest revenue                         |            |            |            |           |            | 631            |
| Interest expense                         |            |            |            |           |            | (1,753)        |
| Total Net Interest                       |            |            |            |           |            | 20,060         |
| Income tax expense                       |            |            |            |           |            | (4,000)        |
| <b>Net Profit for the year</b>           |            |            |            |           |            | <b>16,060</b>  |

The 2010 operating segment note has been restated to be prepared on a consistent basis with the 2011 note, reflecting how Management view the business. This does not materially change any segment revenue or result. The sales from the Australian operations were \$124.578 million (2010: \$130.566 million). The sales from the foreign operations were \$54.778 million (2010: \$58.665 million).

**NOTES TO FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 31 DECEMBER 2011**
**28. EVENTS SUBSEQUENT TO BALANCE DATE**

At the 21 February 2012 Board Meeting, the Directors declared an 8.0 cents fully franked final dividend on ordinary shares in respect of the year ended 31 December 2011. The total amount of this final dividend is \$6.508 million and in accordance with Accounting Standards it has not been provided for in the 31 December 2011 financial statements.

There has not been any other matter or circumstance in the interval between the end of the financial year and the date of this report that has materially affected or may materially affect the operations of the consolidated entity, the results of those operations or the state of affairs of the consolidated entity in subsequent financial periods.

**29. EARNINGS PER SHARE**

|  | 2011<br>\$'000 | 2010<br>\$'000 |
|--|----------------|----------------|
| - Basic earnings per share (cents per share)   | 16.77 cents    | 20.21 cents    |
| - Diluted earnings per share (cents per share) | 16.60 cents    | 20.20 cents    |

The following reflects the income and share data used in the calculations of basic and diluted earnings per share:

|   | 2011<br>\$'000          | 2010<br>\$'000 |
|---|-------------------------|----------------|
| Net Profit attributable to ordinary equity holders of the parent  | 13,524                  | 16,060         |
|   | <b>Number of shares</b> |                |
| Weighted average number of ordinary shares on issue used in the calculation of basic earnings per share | 80,647,185              | 79,473,144     |
| Effect of dilution:   |                         |                |
| Share options   | 840,000                 | 21,940         |
| Adjusted weighted average number of ordinary shares used in calculating diluted earnings per share      | 81,487,185              | 79,495,084     |

There have been no transactions involving ordinary shares or potential ordinary shares that would significantly change the number of ordinary shares or potential ordinary shares outstanding between the reporting date and the date of completion of these financial statements.

Options granted to employees are considered to be potential ordinary shares and have been included in the determination of diluted earnings per share to the extent that they are dilutive. These options have not been included in the determination of basic earnings per share.

|   | CONSOLIDATED   |                |
|---|----------------|----------------|
|   | 2011<br>\$     | 2010<br>\$     |
| <b>30. AUDITORS' REMUNERATION</b>   |                |                |
| Amounts received or due and receivable by the auditors of Melbourne IT Ltd for:                             |                |                |
| - Audit or review of the financial statements of the entity and any other entity in the consolidated entity | 515,298        | 554,000        |
| Other services in relation to the entity and any other entity in the consolidated entity:                   |                |                |
| - Tax Compliance  | 73,178         | 136,487        |
| - Assurance and advisory related  | 24,200         | 30,200         |
|   | <b>612,676</b> | <b>720,687</b> |
| Amounts received or due and receivable by non Ernst & Young audit firms for:                                |                |                |
| - Review of the financial report  | 36,625         | 45,528         |
| - Taxation services   | 16,460         | 17,096         |
| - Other non-audit services  | 14,308         | 9,380          |
|   | <b>67,393</b>  | <b>72,004</b>  |

**31. RELATED PARTY DISCLOSURES**
**Ultimate parent**

The ultimate Australian Parent entity in the wholly owned Group is Melbourne IT Ltd. During the year various intercompany transactions were undertaken between companies in the wholly owned Group. These transactions were undertaken on a net margin basis. The effect of these transactions are fully eliminated on consolidation. All intercompany balances, payable and receivable, are on an "arm's length" basis with standard terms and conditions.

**Other related party transactions**

There were no other transactions with related parties during the year ended 31 December 2011 or 2010 other than detailed within the annual report.

NOTES TO FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 31 DECEMBER 2011

32. DIRECTOR AND EXECUTIVE DISCLOSURES

(a) Details of Key Management Personnel

(i) Directors

|                      |                          |
|----------------------|--------------------------|
| Mr Simon Jones       | Chairman (non-executive) |
| Mr Tom Kiing         | Director (non-executive) |
| Prof. Iain Morrison  | Director (non-executive) |
| Mr Robert Stewart AM | Director (non-executive) |
| Mr Andrew Walsh      | Director (non-executive) |

(ii) Executives

|                        |   |
|------------------------|---|
| Mr Theo Hnarakis       | Managing Director / Chief Executive Officer                             |
| Mr Damian Walsh        | Chief Operating Officer (ceased to hold this position 24 February 2012) |
| Mr Damon Fieldgate     | Executive General Manager - SMB   |
| Ms Lori Harmon         | Executive Vice President - GPS  |
| Ms Ashe-lee Jegathesan | Company Secretary and General Counsel                                   |
| Mr Kanchan Mhatre      | Executive Vice President - DBS  |
| Ms Carolyn Sutton      | Chief Financial Officer (Resigned 23 August 2011)                       |
| Mr Peter Findlay       | Chief Financial Officer (Appointed 17 October 2011)                     |

(b) Remuneration of Key Management Personnel

Compensation of Key Management personnel

|                     | CONSOLIDATED   |                |
|---------------------|----------------|----------------|
|                     | 2011<br>\$'000 | 2010<br>\$'000 |
| Short term benefits | 2,957          | 2,915          |
| Post Employment     | 183            | 198            |
| Long term benefits  | 30             | 30             |
| Share-based Payment | 283            | 155            |
|                     | <u>3,452</u>   | <u>3,298</u>   |

(c) Option holdings of Key Management Personnel (consolidated)

| 2011                   | Balance at 1<br>January 2011 | Granted as<br>Remuneration | Options<br>Exercised /<br>Lapsed | Balance at 31<br>December 2011 | Not Exercisable | Exercisable    |
|------------------------|------------------------------|----------------------------|----------------------------------|--------------------------------|-----------------|----------------|
|                        |                              |                            |                                  |                                |                 |                |
| Mr Theo Hnarakis       | 838,400                      | 185,000                    | (250,000)                        | 773,400                        | 370,000         | 403,400        |
| Mr Damian Walsh        | 75,000                       | 75,000                     | -                                | 150,000                        | 150,000         | -              |
| Ms Lori Harmon         | 50,000                       | 50,000                     | -                                | 100,000                        | 100,000         | -              |
| Mr Damon Fieldgate     | 88,408                       | 50,000                     | -                                | 138,408                        | 100,000         | 38,408         |
| Ms Ashe-lee Jegathesan | 40,000                       | 50,000                     | -                                | 90,000                         | 90,000          | -              |
| Mr Kanchan Mhatre      | 86,816                       | 50,000                     | -                                | 136,816                        | 100,000         | 36,816         |
| Ms Carolyn Sutton (1)  | 50,000                       | -                          | (50,000)                         | -                              | -               | -              |
| Mr Peter Findlay (2)   | -                            | -                          | -                                | -                              | -               | -              |
| <b>Total 2011</b>      | <b>1,228,624</b>             | <b>460,000</b>             | <b>-</b>                         | <b>1,388,624</b>               | <b>910,000</b>  | <b>478,624</b> |

(1) Ms Carolyn Sutton resigned from the executive as Chief Financial Officer on 23 August 2011

(2) Mr Peter Findlay was appointed to the executive as Chief Financial Officer on 17 October 2011

| 2010                   | Balance at 1<br>January 2010 | Granted as<br>Remuneration | Options<br>Exercised /<br>Lapsed | Balance at 31<br>December 2010 | Not Exercisable | Exercisable    |
|------------------------|------------------------------|----------------------------|----------------------------------|--------------------------------|-----------------|----------------|
|                        |                              |                            |                                  |                                |                 |                |
| Mr Theo Hnarakis       | 750,000                      | 185,000                    | (96,600)                         | 838,400                        | 185,000         | 653,400        |
| Mr Damian Walsh        | -                            | 75,000                     | -                                | 75,000                         | 75,000          | -              |
| Ms Lori Harmon         | -                            | 50,000                     | -                                | 50,000                         | 50,000          | -              |
| Mr Damon Fieldgate     | 50,000                       | 50,000                     | (11,592)                         | 88,408                         | 50,000          | 38,408         |
| Ms Ashe-lee Jegathesan | -                            | 40,000                     | -                                | 40,000                         | 40,000          | -              |
| Mr Kanchan Mhatre      | 60,000                       | 50,000                     | (23,184)                         | 86,816                         | 50,000          | 36,816         |
| Ms Carolyn Sutton (1)  | -                            | 50,000                     | -                                | 50,000                         | 50,000          | -              |
| <b>Total 2010</b>      | <b>860,000</b>               | <b>500,000</b>             | <b>(131,376)</b>                 | <b>1,228,624</b>               | <b>500,000</b>  | <b>728,624</b> |

In 2010, a review of the number of employees classed as Key Management Personnel in line with AASB 124 and the Corporations Act was conducted and subsequently revised to exclude the Chief Executive Officers of Enterprise Services and For the Record.

(1) Ms Carolyn Sutton was appointed to the executive as Chief Financial Officer on 1 February 2010

NOTES TO FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 31 DECEMBER 2011

32. DIRECTOR AND EXECUTIVE DISCLOSURES (Continued)

(c) Option holdings of Key Management Personnel (consolidated)

No options were issued to non-executive Directors of Melbourne IT Ltd during the year ended 31 December 2011.

(d) Shareholdings of Key Management Personnel (consolidated)

| 2011                                      | Shares held in Melbourne IT Ltd <sup>^</sup> | Balance as at 1<br>January 2011 | Granted as<br>Remuneration | On Exercise of<br>Options | Net Change<br>Other* | Balance as at 31<br>December 2011 |
|---|--|---------------------------------|----------------------------|---------------------------|----------------------|-----------------------------------|
|   |  |                                 |                            |                           |                      |                                   |
| Mr Simon Jones                            |  | 98,698                          | -                          | -                         | 26,420               | 125,118                           |
| Mr Tom Kiing                              |  | 5,721,488                       | -                          | -                         | -                    | 5,721,488                         |
| Prof. Iain Morrison                       |  | 48,559                          | -                          | -                         | 5,000                | 53,559                            |
| Mr Robert Stewart                         |  | 403,882                         | -                          | -                         | 174,862              | 578,744                           |
| Mr Andrew Walsh                           |  | 48,473                          | -                          | -                         | -                    | 48,473                            |
| Executives                                |  |                                 |                            |                           |                      |                                   |
| Mr Theo Hnarakis                          |  | 687,881                         | -                          | -                         | 244                  | 688,125                           |
| <b>Total 2011</b>                         |  | <b>7,008,981</b>                | <b>-</b>                   | <b>-</b>                  | <b>206,526</b>       | <b>7,215,507</b>                  |
| * On market transactions                  |  |                                 |                            |                           |                      |                                   |
| <sup>^</sup> Direct and indirect holdings |  |                                 |                            |                           |                      |                                   |

| 2010  | Shares held in Melbourne IT Ltd <sup>^</sup> | Balance as at 1<br>January 2010 | Granted as<br>Remuneration | On Exercise of<br>Options | Net Change<br>Other* | Balance as at 31<br>December 2010 |
|---|--|---------------------------------|----------------------------|---------------------------|----------------------|-----------------------------------|
|   |  |                                 |                            |                           |                      |                                   |
| Mr Simon Jones  |  | 92,694                          | -                          | -                         | 6,004                | 98,698                            |
| Mr Tom Kiing  |  | 5,721,488                       | -                          | -                         | -                    | 5,721,488                         |
| Prof. Iain Morrison   |  | 48,559                          | -                          | -                         | -                    | 48,559                            |
| Mr Robert Stewart   |  | 391,964                         | -                          | -                         | 11,918               | 403,882                           |
| Ms Lucy Turnbull (1)  |  | 5,477,694                       | -                          | -                         | (5,477,694)          | -                                 |
| Mr Andrew Walsh   |  | 48,473                          | -                          | -                         | -                    | 48,473                            |
| Executives  |  |                                 |                            |                           |                      |                                   |
| Mr Theo Hnarakis  |  | 687,689                         | -                          | -                         | 192                  | 687,881                           |
| <b>Total 2010</b>   |  | <b>12,468,561</b>               | <b>-</b>                   | <b>-</b>                  | <b>(5,459,580)</b>   | <b>7,008,981</b>                  |
| (1) Ms Lucy Turnbull resigned as a Director on 10 December 2010 and net change in shareholding reflects this resignation from office. |  |                                 |                            |                           |                      |                                   |
| * On market transactions  |  |                                 |                            |                           |                      |                                   |
| <sup>^</sup> Direct and indirect holdings   |  |                                 |                            |                           |                      |                                   |

(e) Other Transactions and Balances with Key Management Personnel

Sales to key management personnel are made at arm's length at normal market prices and on normal commercial terms and are negligible.

**NOTES TO FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 31 DECEMBER 2011**
**33. SHARE OPTIONS**

The Melbourne IT Executive & Employee Option Plans ("ESOP") have been established where the managing director and employees of the company are issued with options over the ordinary shares in Melbourne IT Ltd. The options, issued for nil consideration, are issued in accordance with performance guidelines established by the directors of Melbourne IT Ltd. The options cannot be transferred and will not be quoted on the ASX. The managing director and all full-time or permanent part-time employees of the company or any of its related body corporate are eligible to participate in the option plans.

During the year 92,900 (2010: 174,400) options under the Melbourne IT Executive & Employee Option Plans were exercised at an average price of \$1.67 (2010: \$1.21), with a total cash consideration received by Melbourne IT Ltd of \$155,143 (2010: \$211,856).

Each option is to subscribe for one fully paid Share. When issued, the Share will rank equally with other Shares. The options are not transferable except to the legal personal representative of a deceased or legally incapacitated option holder. The options are issued for a term of 5 years.

Under the Option Plans, the options have other terms specified at the time the options are offered. These terms differ between the Managing Director, senior executives and general employees. The terms may include conditions, which set out the number or percentage of options able to be exercised at certain time periods or under certain circumstances. For the managing director and senior executives, performance conditions may require that the number of options able to be exercised be reduced or that some or all of the options lapse under specified circumstances.

The Board has adopted certain policies concerning the terms of the options to be granted under the Option Plans. The Board has the absolute discretion to change these policies at any time, although any change in its policies will have an effect only on options that are issued at or after the time of the change.

The expected life of the options is based on historical data and is not necessarily indicative of exercise patterns that may occur. The expected volatility reflects the assumptions that the historical volatility is indicative of future trends, which may also not necessarily be the actual outcome.

**(a) Options held at the beginning of the reporting period:**

The following table summarises information about options held by directors and employees as at 1 January 2011:

| Number of Options | Grant Date | Vesting Date | Expiry Date | Weighted Average Exercise Price |
|-------------------|------------|--------------|-------------|---------------------------------|
| 98,700            | 28/04/06   | 28/04/07     | 28/04/11    | \$ 1.67                         |
| 524,200           | 17/07/06   | 17/07/08     | 17/07/11    | \$ 1.85                         |
| 1,188,400         | 27/04/07   | 27/04/09     | 27/04/12    | \$ 3.42                         |
| 177,066           | 11/09/07   | 11/09/09     | 11/09/12    | \$ 3.60                         |
| 1,592,064         | 18/07/08   | 18/07/10     | 18/07/13    | \$ 3.06                         |
| 142,224           | 19/08/08   | 19/08/10     | 19/08/13    | \$ 3.06                         |
| 469,000           | 24/10/08   | 24/10/10     | 24/10/13    | \$ 2.12                         |
| 190,000           | 1/07/10    | 1/07/13      | 1/07/13     | \$ -                            |
| 720,000           | 1/07/10    | 1/07/13      | 1/07/13     | \$ -                            |
| 5,101,654         |            |              |             | \$ 2.38                         |

As at 1 January 2011, 4,191,654 shares were exercisable.

**(b) Options granted during the reporting period**

In the year ended 31 December 2011 930,000 (2010:910,000) options were granted over ordinary shares.

| 2011                        | 1-Jul-11<br>Equity Settled | 31-Dec-11<br>Cash Settled |
|-----------------------------|----------------------------|---------------------------|
| Number of Options           | 710,000                    | 220,000                   |
| Grant date                  | 1/07/2011                  | 1/07/2011                 |
| First Vesting date          | 1/07/2014                  | 1/07/2014                 |
| Weighted Average Fair Value | 1.24                       | 1.27                      |
| Expected Volatility         | 38.0%                      | 27.5%                     |
| Risk-free interest rate     | 4.8%                       | 4.3%                      |
| Expected life of option     | 2.5 years                  | 2.5 years                 |
| Dividend yield              | 7.8%                       | 9.7%                      |

The following table summarises the movement in share options issued during the year:

|  | 2011 Number | 2010 Number |
|--|-------------|-------------|
| Outstanding at the beginning of the year | 5,101,654   | 5,204,235   |
| Granted during the year                  | 930,000     | 910,000     |
| Exercised during the year                | (92,900)    | (174,400)   |
| Lapsed during the year                   | (989,650)   | (838,181)   |
| Outstanding at year end                  | 4,949,104   | 5,101,654   |

**NOTES TO FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 31 DECEMBER 2011**
**33. SHARE OPTIONS (Continued)**
**(c) Options exercised during the reporting period**

The following table summarises information about options exercised by employees during the year ended 31 December 2011:

| No. of Options | Grant Date | Vesting Date | Expiry Date | Weighted Average Exercise Price | Issue Date | Fair Value of Shares Issued (1) |
|----------------|------------|--------------|-------------|---------------------------------|------------|---------------------------------|
| 4,900          | 28/04/2006 | 28/04/2006   | 28/04/2011  | \$ 1.67                         | 28/04/2011 | \$ 1.89                         |
| 5,000          | 28/04/2006 | 28/04/2006   | 28/04/2011  | \$ 1.67                         | 28/01/2011 | \$ 1.95                         |
| 7,000          | 28/04/2006 | 28/04/2006   | 28/04/2011  | \$ 1.67                         | 28/01/2011 | \$ 1.95                         |
| 7,000          | 28/04/2006 | 28/04/2006   | 28/04/2011  | \$ 1.67                         | 28/04/2011 | \$ 1.89                         |
| 25,695         | 28/04/2006 | 28/04/2006   | 28/04/2011  | \$ 1.67                         | 21/04/2011 | \$ 1.88                         |
| 14,305         | 28/04/2006 | 28/04/2006   | 28/04/2011  | \$ 1.67                         | 27/04/2011 | \$ 1.88                         |
| 15,000         | 28/04/2006 | 28/04/2006   | 28/04/2011  | \$ 1.67                         | 28/04/2011 | \$ 1.89                         |
| 7,000          | 28/04/2006 | 28/04/2006   | 28/04/2011  | \$ 1.67                         | 28/04/2011 | \$ 1.89                         |
| 7,000          | 28/04/2006 | 28/04/2006   | 28/04/2011  | \$ 1.67                         | 21/04/2011 | \$ 1.88                         |
| 92,900         |            |              |             | \$ 1.67                         |            |                                 |

(1) Fair values of shares during the reporting period is estimated to be the market prices of shares in Melbourne IT Limited on the ASX as at the close of trading on their respective issue dates net of brokerage fee.

During the year cash received from options exercised was \$0.155 million (2010: \$0.212 million).

The following table summarises information about options exercised by directors and employees during the year ended 31 December 2010:

| No. of Options | Grant Date | Vesting Date | Expiry Date | Weighted Average Exercise Price | Issue Date | Fair Value of Shares Issued (1) |
|----------------|------------|--------------|-------------|---------------------------------|------------|---------------------------------|
| 2,800          | 22/04/2005 | 22/10/2005   | 22/04/2010  | \$ 1.28                         | 4/01/2010  | \$ 1.74                         |
| 7,000          | 22/04/2005 | 22/10/2005   | 22/04/2010  | \$ 1.28                         | 1/03/2010  | \$ 1.83                         |
| 20,000         | 22/04/2005 | 22/10/2005   | 22/04/2010  | \$ 1.28                         | 14/04/2010 | \$ 1.73                         |
| 2,800          | 22/04/2005 | 22/10/2005   | 22/04/2010  | \$ 1.28                         | 21/04/2010 | \$ 1.88                         |
| 5,000          | 22/04/2005 | 22/10/2005   | 22/04/2010  | \$ 1.28                         | 21/04/2010 | \$ 1.88                         |
| 8,000          | 22/04/2005 | 22/10/2005   | 22/04/2010  | \$ 1.28                         | 21/04/2010 | \$ 1.88                         |
| 5,000          | 28/10/2005 | 28/10/2006   | 28/10/2010  | \$ 1.16                         | 5/02/2010  | \$ 1.60                         |
| 13,000         | 28/10/2005 | 28/10/2006   | 28/10/2010  | \$ 1.16                         | 1/03/2010  | \$ 1.83                         |
| 16,000         | 28/10/2005 | 28/10/2006   | 28/10/2010  | \$ 1.16                         | 8/04/2010  | \$ 1.73                         |
| 2,000          | 28/10/2005 | 28/10/2006   | 28/10/2010  | \$ 1.16                         | 28/10/2010 | \$ 1.83                         |
| 2,800          | 28/10/2005 | 28/10/2006   | 28/10/2010  | \$ 1.16                         | 28/10/2010 | \$ 1.83                         |
| 5,000          | 28/10/2005 | 28/10/2006   | 28/10/2010  | \$ 1.16                         | 28/10/2010 | \$ 1.83                         |
| 5,000          | 28/10/2005 | 28/10/2006   | 28/10/2010  | \$ 1.16                         | 28/10/2010 | \$ 1.83                         |
| 7,000          | 28/10/2005 | 28/10/2006   | 28/10/2010  | \$ 1.16                         | 28/10/2010 | \$ 1.83                         |
| 15,000         | 28/10/2005 | 28/10/2006   | 28/10/2010  | \$ 1.16                         | 28/10/2010 | \$ 1.83                         |
| 16,000         | 28/10/2005 | 28/10/2006   | 28/10/2010  | \$ 1.16                         | 28/10/2010 | \$ 1.83                         |
| 24,000         | 28/10/2005 | 28/10/2006   | 28/10/2010  | \$ 1.16                         | 28/10/2010 | \$ 1.83                         |
| 8,000          | 28/04/2006 | 28/04/2007   | 28/04/2011  | \$ 1.67                         | 16/03/2010 | \$ 1.85                         |
| 174,400        |            |              |             | 1.21                            |            |                                 |

(1) Fair values of shares during the reporting period is estimated to be the market prices of shares in Melbourne IT Limited on the ASX as at the close of trading on their respective issue dates.

**(d) Options lapsed or forfeited during the reporting period:**

A total of 989,650 (2010: 838,181) options lapsed or were forfeited with a weighted average exercise price of \$2.00 (2010: \$2.97), by directors and employees during the year ended 31 December 2011.

**(e) Options held at the end of the reporting period:**

The following table summarises information about options held by directors and employees as at 31 December 2011:

| Number of Options | Grant Date | Vesting Date | Expiry Date | Weighted Average Exercise Price |
|-------------------|------------|--------------|-------------|---------------------------------|
| 1,111,000         | 27/04/07   | 27/04/09     | 27/04/12    | \$ 3.42                         |
| 177,066           | 11/09/07   | 11/09/09     | 11/09/12    | \$ 3.60                         |
| 1,433,814         | 18/07/08   | 18/07/10     | 18/07/13    | \$ 3.06                         |
| 142,224           | 19/08/08   | 19/08/10     | 19/08/13    | \$ 3.06                         |
| 405,000           | 24/10/08   | 24/10/10     | 24/10/13    | \$ 2.12                         |
| 180,000           | 1/07/10    | 1/07/13      | 1/07/13     | \$ -                            |
| 610,000           | 1/07/10    | 1/07/13      | 1/07/13     | \$ -                            |
| 180,000           | 1/07/11    | 1/07/14      | 1/07/14     | \$ -                            |
| 710,000           | 1/07/11    | 1/07/14      | 1/07/14     | \$ -                            |
| 4,949,104         |            |              |             | \$ 2.04                         |

As at 31 December 2011, 3,269,104 shares were exercisable.



**NOTES TO FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 31 DECEMBER 2011**

**33. SHARE OPTIONS (Continued)**

**(f) Weighted average remaining contractual life**

The weighted average remaining contractual life for the share options outstanding as at 31 December 2011 is 1.43 years (2010: 2.00 years).

**(g) Option pricing model: Performance Options Plan and Long Term Incentive Deferred Cash Bonus Plan**

The fair value of the equity-settled share based payments granted under the Performance Options Plan is estimated as at the date of grant using a combination of the Black-Scholes methodology (for market based vesting conditions) and discounted cashflow approach (for non-market based vesting conditions).

The following table lists the inputs to the models used for the year ended 31 December 2011:

|                         | <b>Performance<br/>Options Plan</b> | <b>Long Term<br/>Incentive<br/>Deferred Cash<br/>Bonus Plan</b> |
|-------------------------|-------------------------------------|---|
| Dividend yield          | 7.8%                                | 9.7%  |
| Expected volatility     | 38.0%                               | 27.5%   |
| Risk-free interest rate | 4.8%                                | 4.3%  |

The dividend yield is based on historic and future yield estimates. The expected volatility was determined using the group's 5 year share price. The risk-free rate is derived from the yield on Australian Government Bonds of an appropriate term.

**34. INFORMATION RELATING TO MELBOURNE IT LTD ("the parent entity")**

|   | <b>2011<br/>\$'000</b> | <b>2010<br/>\$'000</b> |
|---|------------------------|------------------------|
| Current assets                                  | 21,080                 | 23,826                 |
| Total assets                                    | 142,627                | 140,744                |
| Current liabilities                             | 49,538                 | 52,870                 |
| Total liabilities                               | 63,507                 | 67,965                 |
| Contributed equity                              | 66,900                 | 64,839                 |
| Options reserve                                 | 4,113                  | 3,826                  |
| Hedging reserve                                 | 127                    | 460                    |
| Retained earnings                               | 7,980                  | 3,654                  |
|   | <b>79,120</b>          | <b>72,779</b>          |
| Profit of parent entity                         | 16,376                 | 9,430                  |
| Total comprehensive income of the parent entity | 16,043                 | 9,802                  |

The parent has issued the following guarantees in relation to the debts of its subsidiaries:

-Pursuant to Class Order 98/1418, Melbourne IT Ltd, WebCentral Group Pty Ltd, WebCentral Pty Ltd and For The Record Pty Ltd have entered into a Deed of Cross Guarantee. The effect of the deed is that Melbourne IT Ltd has guaranteed to pay any deficiency in the event of winding up of any controlled entity or if they do not meet their obligations under the terms of overdrafts, loans, leases or other liabilities subject to the guarantee. The controlled entities have also given a similar guarantee in the event that Melbourne IT Ltd is wound up or if it does not meet its obligations under the terms of overdrafts, loans, leases or other liabilities subject to the guarantee.

**NOTES TO FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 31 DECEMBER 2011**

**34. INFORMATION RELATING TO MELBOURNE IT LTD ("the parent entity") (Continued)**

The consolidated financial statements include the financial statements of Melbourne IT Ltd and the subsidiaries in the following table:

| <b>Name</b>                             | <b>Country of<br/>Incorporation</b> | <b>% Equity Interest</b> |             | <b>Cost of Investment \$000</b> |                |
|---|-------------------------------------|--------------------------|-------------|---------------------------------|----------------|
|   |                                     | <b>2011</b>              | <b>2010</b> | <b>2011</b>                     | <b>2010</b>    |
| WebCentral Group Pty Ltd                | (a) Australia                       | 100                      | 100         | 78,190                          | 78,190         |
| Internet Names Worldwide Espana SL      | (a) Spain                           | 100                      | 100         | 5                               | 5              |
| Melbourne IT DBS Group AB               | (a) Sweden                          | 100                      | 100         | 4,663                           | 4,663          |
| Domainz Ltd                             | (a) New Zealand                     | 100                      | 100         | 1,671                           | 1,671          |
| Internet Names Worldwide (US), Inc      | (a) USA                             | 100                      | 100         | 1                               | 1              |
| Melbourne IT GP Holdings Pty Ltd        | (a) Australia                       | 100                      | 100         | -                               | -              |
| Melbourne IT General Partnership        | (b) USA                             | 100                      | 100         | 16,313                          | 16,334         |
| Melbourne IT Digital Brand Services Inc | (b) USA                             | 100                      | 100         | 5,109                           | 5,116          |
| Melbourne IT DBS Group AB               | (b) Sweden                          | 100                      | 100         | 2,217                           | 2,257          |
| Melbourne IT DBS Limited                | (b) UK                              | 100                      | 100         | 1,695                           | 1,699          |
| Advantate Pty Ltd                       | Australia                           | 100                      | 100         | -                               | -              |
|   |                                     |                          |             | <b>109,864</b>                  | <b>109,935</b> |

(a) Investments in controlled entities are initial capital investments and are eliminated in the consolidated financial statements.

(b) Investments in foreign entities are revalued to the year end foreign exchange spot rates.

**35. CONTINGENT LIABILITY**

The Group is subject to claims from time to time in the ordinary course of business. There are currently no claims against the Group of individual significance.

**36. CLOSED GROUP CLASS ORDER DISCLOSURES**

**Entities subject to class order relief**

Pursuant to Class Order 98/1418, relief has been granted to Melbourne IT Ltd, WebCentral Group Pty Ltd, WebCentral Pty Ltd and For The Record Pty Ltd from the *Corporations Act 2001* requirements for the preparation, audit and lodgement of their financial reports.

The consolidated statement of comprehensive income and statement of financial position of the entities that are members of the Closed Group are as follows:

**Consolidated statement of comprehensive income**

|  | <b>Closed group</b>    |                        |
|--|------------------------|------------------------|
|  | <b>2011<br/>\$'000</b> | <b>2010<br/>\$'000</b> |
| Profit before income tax                         | 13,218                 | 15,892                 |
| Income tax expense                               | (2,168)                | (2,949)                |
| Profit after tax, net profit for the period      | 11,050                 | 12,943                 |
| Retained earnings at the beginning of the period | 25,779                 | 24,726                 |
| Dividends provided for or paid                   | (10,144)               | (10,268)               |
| Dividend reinvestment plan                       | (1,906)                | (1,622)                |
| Retained earnings at the end of the period       | <b>24,779</b>          | <b>25,779</b>          |

NOTES TO FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 31 DECEMBER 2011

36. CLOSED GROUP CLASS ORDER DISCLOSURES (Continued)

Consolidated statement of financial position

|   | Closed group   |                |
|---|----------------|----------------|
|   | 2011<br>\$'000 | 2010<br>\$'000 |
| <b>ASSETS</b>                               |                |                |
| <b>Current assets</b>                       |                |                |
| Cash and cash equivalents                   | 8,586          | 13,180         |
| Trade and other receivables                 | 14,027         | 12,487         |
| Inventories                                 | 70             | 76             |
| Prepayments of domain name registry charges | 8,107          | 9,193          |
| Derivatives financial instruments           | 14             | 258            |
| Other assets                                | 2,217          | 2,548          |
| <b>Total current assets</b>                 | <b>33,021</b>  | <b>37,742</b>  |
| <b>Non-current assets</b>                   |                |                |
| Other financial assets                      | 31,686         | 31,757         |
| Property, plant and equipment               | 4,381          | 6,351          |
| Intangible assets                           | 85,633         | 80,040         |
| Deferred tax assets                         | 3,065          | 3,285          |
| Current tax asset                           | 282            | -              |
| Prepayments of domain name registry charges | 6,408          | 7,442          |
| Other assets                                | 56             | 43             |
| <b>Total non-current assets</b>             | <b>131,511</b> | <b>128,918</b> |
| <b>TOTAL ASSETS</b>                         | <b>164,532</b> | <b>166,660</b> |
| <b>LIABILITIES</b>                          |                |                |
| <b>Current liabilities</b>                  |                |                |
| Trade and other payables                    | 15,856         | 10,909         |
| Provisions                                  | 3,839          | 3,406          |
| Current tax liabilities                     | -              | 1,006          |
| Income received in advance                  | 22,586         | 25,984         |
| <b>Total current liabilities</b>            | <b>42,281</b>  | <b>41,305</b>  |
| <b>Non-current liabilities</b>              |                |                |
| Interest-bearing loans and borrowings       | 13,365         | 16,334         |
| Deferred tax income liability               | 130            | 169            |
| Provisions                                  | 810            | 714            |
| Income received in advance                  | 13,662         | 14,805         |
| <b>Total non-current liabilities</b>        | <b>27,967</b>  | <b>32,022</b>  |
| <b>TOTAL LIABILITIES</b>                    | <b>70,248</b>  | <b>73,327</b>  |
| <b>NET ASSETS</b>                           | <b>94,284</b>  | <b>93,333</b>  |
| <b>EQUITY</b>                               |                |                |
| Contributed equity                          | 66,900         | 64,839         |
| Foreign currency translation reserve        | (1,635)        | (1,571)        |
| Options reserve                             | 4,113          | 3,826          |
| Hedging reserve                             | 127            | 460            |
| Retained earnings                           | 24,779         | 25,779         |
| <b>TOTAL EQUITY</b>                         | <b>94,284</b>  | <b>93,333</b>  |

NOTES TO FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 31 DECEMBER 2011

ASX ADDITIONAL INFORMATION

Additional information required by the Australian Stock Exchange and not shown elsewhere in this report is as follows. The below information is current as at 21 February 2012.

(a) Distribution of equity securities

|  | Number of<br>Holders | Number of<br>Shares |
|--|----------------------|---------------------|
| 1-1,000  | 1,762                | 1,024,153           |
| 1,001-5,000  | 2,984                | 7,883,773           |
| 5,001-10,000   | 971                  | 7,360,755           |
| 10,001-100,000   | 839                  | 19,633,188          |
| 100,001 – and over   | 60                   | 45,450,309          |
| <b>Total</b>   | <b>6,616</b>         | <b>81,352,178</b>   |
| The number of shareholders holding less than a marketable parcel of shares are | 500                  | 82,750              |

(b) Twenty largest stakeholders

|   | Number of<br>shares | Percentage of<br>ordinary shares |
|---|---------------------|----------------------------------|
| The names of the twenty largest holders of quoted shares are: |                     |                                  |
| HSBC Custody Nominees (Australia) Limited                     | 11,319,331          | 13.91%                           |
| Wilcrow Pty Limited   | 4,647,840           | 5.71%                            |
| Reckon Limited  | 4,000,897           | 4.92%                            |
| Sieana Pty Ltd  | 3,083,340           | 3.79%                            |
| York Investments Limited                                      | 2,533,823           | 3.11%                            |
| National Nominees Limited                                     | 2,529,483           | 3.11%                            |
| Citicorp Nominees Pty Limited                                 | 2,488,651           | 3.06%                            |
| J P Morgan Nominees Australia Limited                         | 2,369,171           | 2.91%                            |
| Dulwich Storage Company Limited                               | 1,187,451           | 1.46%                            |
| Cogent Nominees Pty Limited                                   | 1,061,513           | 1.30%                            |
| Sandhurst Trustees Ltd  | 1,034,943           | 1.27%                            |
| Turnbull & Partners Pty Limited                               | 781,696             | 0.96%                            |
| Mr Theo Hnarakis & Mrs Sandra Anne Hnarakis                   | 685,405             | 0.84%                            |
| Equitas Nominees Pty Limited                                  | 651,800             | 0.80%                            |
| Mount IDA Holdings Pty Ltd                                    | 526,331             | 0.65%                            |
| RBC Dexia Investor Services Australia Nominees Pty Limited    | 325,713             | 0.40%                            |
| Principal Funds Management Co Pty Ltd                         | 300,000             | 0.37%                            |
| Esteville Nominees Pty Ltd                                    | 296,862             | 0.36%                            |
| Toner Holdings Limited  | 290,146             | 0.36%                            |
| Forsyth Barr Custodians Limited                               | 290,049             | 0.36%                            |
|   | <b>40,404,445</b>   | <b>49.65%</b>                    |

(c) Voting rights

All ordinary shares carry one vote per share without restriction.

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## MELBOURNE IT LTD

ABN: 21 073 716 793

## DIRECTORS

Mr. S.D. Jones (Chairman)  
Mr. T.J. Hnarakis (Managing Director)  
Mr. T. Kiing  
Prof. I. Morrison  
Mr. R.J. Stewart  
Mr. A. Walsh

## SHARE REGISTRY

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Melbourne, Victoria, 3000  
Tel: +61 3 9615 9800  
Fax: +61 3 9615 9900

## MANAGING DIRECTOR AND CHIEF EXECUTIVE OFFICER

Mr. T.J. Hnarakis

## CHIEF OPERATING OFFICER

Mr. D.M. Walsh

## CHIEF FINANCIAL OFFICER

Mr P. Findlay (Appointed 17 October 2011)  
Mr. B. Smart (Appointed Acting Chief Financial Officer 24 August 2011  
and resigned 16 October 2011)  
Ms C. Sutton (Resigned 23 August 2011)

## COMPANY SECRETARY

Ms. A. Jegathesan

## AUDITORS

Ernst & Young

## IMPORTANT INFORMATION FOR SHAREHOLDERS

In 2011, Melbourne IT has produced two shareholder documents – an Annual Review and an Annual Report. The Annual Review is a more succinct shareholder overview designed to provide a high level summary of the strategic and operational performance of the company during 2011. The Annual Report cannot be expected to provide as full an understanding of the financial performance, financial position and investing activities of the company as the Annual Report.

In addition to the information in the Annual Review, the Annual Report contains a full financial report and our auditors' report. Shareholders wishing to receive a copy of the more detailed Annual Report may do so by visiting <http://annualreport.melbourneit.info>

The Annual Review can also be accessed online at <http://annualreport.melbourneit.info>

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